Gandhi Memorial College Of Education Bantalab Jammu

25th Successful Edition

INCOME TAX
LAW AND PRACTICE

V.P. GAUR
D.B. NARANG

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LAW AND PRACTICE

(1997-98)

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By the same Authors

1. आयकर विधान एवं अभ्यास (संस्करण १९९७)
2. Lectures on Punjab General Sales Tax Act, 1948 and Central Sales Tax Act, 1956
3. Practical Income Tax (12th revised edition 1997)
4. Lectures on Delhi Sales Tax Act and Central Sales Tax Act.
5. Wealth Tax, Gift Tax and Central Sales Tax Act (8th Edition 1997)
6. Kalyani's Income-tax Made Easy for Salaries (10th Edition 1997-98)

Note: *Figures and words (e.g. P. 12) appearing at the end of some of the unsolved questions in this book relate to corresponding number of the solution given in respective chapter of the book (Practical Income-tax).*

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INCOME TAX

LAW AND PRACTICE

[INCORPORATING INCOME-TAX ACT, 1961 AS AMENDED UP-TO-DATE]

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PREFACE

(25th Edition)

We express our profound gratitude to all our patrons—students, Teachers, Income-tax practitioners, Chartered Accountants and General Public, whose tremendous response over last 25 years has helped us to bring 25th (Silver Jubilee) Edition of this Book. This edition, which is being published in new size and new matter, is expected to meet the new expectations of our patrons.

The fate of Income tax is dependant on the fate of our political system. The changes in this Act coincide with the whims and policies of our political parties and the outlook of our Finance Minister. This year's political storm made the people of India to wait and see the fate of the "Dream Budget". Ultimately storm blew over and the budget including the Finance Act has been passed. The amendments made by the Finance Act 1997 have been incorporated in the main text of this book.

We have made our effort on the basis of amendments, Circulars, Notifications, Court rulings etc. We shall continue our efforts to make this book simple and understandable not only for professionals but also for those people who do not know anything about this subject.

Our sincere thanks to Sh. Raj Kumar and his team of Kalyani Publishers for their 25 years of nice and healthy co-operation in bringing out this book.

1st June, 1997

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PREFACE

(First Edition)

From time to time attempts are being made to rationalise and simplify the Income-Tax Act, 1961. Amendments through the Finance Act are also being made every year by the Finance Minister while presenting the budget proposals. The result of frequent amendments is that it is very difficult to know correctly the Income-tax Act and Rules framed thereunder. The successive amendments make the law more and more complicated. Thus, there is a positive need for a book which may present the law and practice of income-tax in an analytical and lucid manner, illustrated with suitable examples so that the reader may follow it step by step without any difficulty. *Income Tax Law and Practice* has been written to achieve this objective and is intended to be useful for B.Com. (Pass & Hons.), M.Com., University Examinations as well as examinations conducted by the Income-tax Department and professional institutes.

The book has been made up-to-date in the light of recent amendments made in the Income-tax Act including the recent case laws on the subject. Many examples and illustrations specially prepared and selected from various academic and professional examinations, have been given with explanatory notes to make the law and practice of Income-tax more clear. To give a better understanding of the subject, theoretical questions (which give the latest trend in examinations) have been given at the end of each chapter.

We are thankful to our friends and students for helping us in completing the work.

The writers will feel amply rewarded for their labour if the book is found useful by the students for whom it has been written.

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Rates of Tax

[Assessment year 1997-98]

I. For Individual, H.U.F., Association of Persons, Body of Individuals

First Rs. 40,000 of Total Income	NIL
Next Rs. 20,000 of Total Income	15%
Next Rs. 60,000 of Total Income	30%
Above Rs. 1,20,000 of Total Income	40%
II. Maximum Marginal Rate	**40%**

Assessment year 1998-99

I. First Rs. 40,000 of Total Income	NIL
Next Rs. 20,000 of Total Income	10%
Next Rs. 90,000 of Total Income	20%
Excess over Rs. 1,50,000 of Total Income	30%
II. Maximum Marginal Rate	**30%**

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PART I

INTRODUCTION

1. BASIC CONCEPTS
2. AGRICULTURAL INCOME AND ITS ASSESSMENT
3. CAPITAL AND REVENUE
4. BASIS OF CHARGE
5. EXEMPTED INCOMES

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"An assessee can so arrange his affairs as to minimise his tax burden."

[C.I.T. v. Calcutta Discount Co. Ltd. (1973) (S.C.)]

Tax evasion is illegal but tax avoidance is in no way a crime.

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1 BASIC CONCEPTS

Importance—History—Definitions—Assessee—Person—Income—Assessment year—Previous year—Exceptions—Questions.

IMPORTANCE

The taxes levied by the Government form a pool of resources to be used for the collective benefit of the public. The taxation is an exercise in the collective solution of individual problems. The state takes upon itself the duty of solving the problems of the underprivileged and needs finance for this purpose. The Government can mobilise resources by imposing taxes on the privileged ones.

The taxation structure of the country can play a very important role in the working of our economy. Some time back the emphasis was on higher rates of tax and more incentives. But recently the emphasis has shifted to decrease in rates of taxes and withdrawal of incentives. While designing the taxation structure it has to be seen that it is in conformity with our economic and social objectives. It should not impair the incentives to personal savings and investment flow and on the other hand it should not result into decrease in revenue for the state.

In our present day economic structure income-tax plays a vital role as a source of revenue and a measure of removal of economic disparity. Our taxation structure provides for two types of taxes—direct and indirect; the income tax, wealth tax and gift tax are direct taxes whereas sales tax and excise duties are indirect taxes.

HISTORY

The income-tax was introduced in India for the first time in 1860 by British rulers following the mutiny of 1857. The period between 1860 to 1886 was a period of experiments in the context of income-tax. This period ended in 1886 when first Income-tax Act came into existence. The pattern laid down in it for levying of tax continues to operate even to-day though in some changed form. In 1918 another Act—Income-tax Act, 1918 was passed but it was short lived and was replaced by Income-tax Act, 1922 and it remained in existence and operation till 31st March, 1961.

PRESENT ACT

On the recommendation of Law Commission & Direct Taxes Enquiry Committee and in consultation with Law Ministry a bill was framed. This bill was referred to

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a select committee and finally passed in Sept. 1961. This Act came into force from 1st April 1962 in whole of the country.

Income-tax Act, 1961 is a comprehensive Act and consists of 298 sections, sub-sections running into thousands, schedules, rules, sub-rules, etc. and is supported by other Acts and rules. This Act has been amended by several amending Acts since 1961. The annual Finance Bills presented to Parliament alongwith budget make far-reaching amendments in this Act every year.

CONCEPT OF TOTAL INCOME

Under section 2(45) '*Total income*' means the total amount of income referred to in section 5, and computed in the manner laid down in this Act.

According to this Act, income of a person is computed in *five* parts and each part is known as head of income. These heads are :

(*i*) Income under the head '*salaries*' ;

(*ii*) Income from *House property* ;

(*iii*) Income under the head *Profits and gains of business or profession* ;

(*iv*) Income under the head *Capital gains* ; and

(*v*) Income from *Other sources*.

Total of incomes computed under these heads is called *Gross Total Income* (G.T.I.) and out of this deductions u/s 80 are allowed. The resultant figure is called *Total Income* on which rates of tax are applied.

DEFINITIONS

1. Agricultural Income [Section 2(1A)]

Agricultural income is fully exempted from tax u/s 10(1) and as such does not form part of total income. Due to its importance, the concept of Agricultural Income and its present treatment has been discussed in detail in next chapter.

2. Assessee [Section 2(7)]

'Assessee' means a person by whom any tax or any other sum of money is payable under this Act and includes—

(a) every person in respect of whom any proceedings under this Act have been taken for the assessment of his income or of the income of any other person in respect of which he is assessable or loss sustained by him or by such other person or of the amount of refund due to him or to such person;

(b) every person who is deemed to be an assessee under any provision of this Act;

(c) every person who is deemed to be an assessee-in-default under any provision of this Act.

The above definition divides various types of assessees into three categories :

(*a*) *ordinary assessee*—it includes

(*i*) any person against whom some proceedings under this Act are going on. It is immaterial whether any tax or other amount is payable by him or not ;

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(*ii*) any person who has sustained loss and has filed return of loss u/s 139(3) ;

(*iii*) any person by whom some amount of interest, tax or penalty is payable under this Act ; or

(*iv*) any person who is entitled to refund of tax under this Act.

(*b*) *representative assessee or deemed assessee.* A person may not be liable only for his own income or loss but also on the income or loss of other persons *e.g.* guardian of minor or lunatic, agent of a non-resident etc. In such case the persons responsible for the assessment of income of such persons are called *representative assessees.* Such person is *deemed to be an assessee.*

(*c*) *assessee-in-default.* A person is deemed to be an assessee-in-default if he fails to fulfil his statutory obligations. In case of an employer paying salary or a persor who is paying interest it is their duty to deduct tax at source and deposit the amount of tax so collected in Government treasury. If he fails to deduct tax at source or deducts tax but does not deposit it in the treasury, he is known as assessee-in-default.

3. Average Rate [Section 2(10)]

"average rate of income-tax" means the rate arrived at by dividing the amount of income-tax calculated on the total income by such total income.

$$\text{Average rate} = \frac{\text{Total Tax}}{\text{Total Income}} \times 100$$

Maximum Marginal Rate [MMR] (Section 167B (Expl. 2)]

It means the rate of tax for an individual, which is applicable on highest slab of income. At present for assessment year 1997-98 it is 40%.

4. Charitable purpose [Section 2(15)]

"Charitable purpose" includes relief of the poor, education, medical relief and the advancement of any other object of general public utility.

5. Child [Section 2(15A)]

"Child" in relation to an individual, includes a step-child and an adopted child of that individual. It includes both male and female children.

6. Fair Market Value [Section 2(22)]

The "fair market value" in relation to a capital asset means—

(*a*) the price that the capital asset would ordinarily fetch on sale in the open market on the relevant date; and

(*b*) where the price referred to in sub-clause (i) is not ascertainable, such price as may be determined in accordance with the rules made under this Act.

7. Person [Section 2(31)]

Person includes:

(i) an Individual;

(ii) a Hindu Undivided Family;

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(iii) a Company;

(iv) a Firm;

(v) an association of persons or a body of individuals, whether incorporated or not;

(vi) a local authority; and

(vii) every artificial juridical person not falling within any of the preceding sub-clauses.

The word person is a very wide term and embraces in itself the following:

(i) *Individual.* It refers to a natural human being whether male or female, minor or major.

(ii) *Hindu Undivided Family.* It is a relationship created due to operation of Hindu Law. The manager of HUF is called *"Karta"* and its members are called *'Coparceners'*.

(iii) *Company.* It is an artificial person registered under Indian Companies Act 1956 or any other law.

(iv) *Firm.* It is an entity which comes into existence as a result of partnership agreement. The Income tax Act accepts only these entities as *firms* which are assessed as firms under section 184 of the Act. The only condition for a partnership entity to be assessed as firm is that it must submit its instrument of partnership (partnership deed) duly authenticated by all partners except a minor partner and it must specify the shares of the partners.

(v) *Association of Persons or Body of Individuals.* Co-operative societies, MARKFED, NAFED etc. are the examples of such persons. When persons combine togather to carry on a joint enterprise and they do not constitute partnership under the ambit of law, they are assessable as an association of persons. Receiving income jointly is not the only feature of an association of persons. There must be common purpose, and common action to achieve common purpose *i.e.* to earn income. An A.O.P. can have firms, companies, associations and individuals as its members.

A body of individuals (B.O.I) cannot have non-individuals as its members. Only natural human beings can be members of a body of individuals.

Whether a particular group is A.O.P. or B.O.I. is a question of fact to be decided in each case separately.

(vi) *Local Authority.* Municipality, Panchayat, Cantonment Board, Port Trust etc. are called local authorities.

(vii) *Artificial Juridical Person.* Statutory Corporations like Life Insurance Corporation, a University etc. are called artificial juridical persons.

8. *Income* [Section 2(24)]

"Income includes"

(i) Profits and gains ;

(ii) Dividend;

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(iia) Any voluntary contributions received by a charitable or religious trust or other institution (except in case where such contributions have been received with a specific direction that these sums would form part of the corpus of the trust or institution);

(iii) The value of any perquisite or profit in lieu of salary taxable under clauses (2) and (3) of section 17;

(iiia) Any special allowance or benefit, other than perquisite included under sub-clause (iii), specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit;

(iiib) Any allowance granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at a place where he ordinarily resides or to compensate him for the increased cost of living;

(iv) Value of any benefit or amenity, whether convertible into money or not, obtained by a representative assessee or by any person on whose behalf such benefit is received by representative assessee and sum paid by representative assessee in respect of any obligation which but for such payment would have been payable by the person on whose behalf representative assessee has made such payment [Inserted by Finance Act (2) 1980];

(iva) The value of any benefits or perquisites, whether convertible into money or not, obtained from a company either by a director or by a person, who has a substantial interest in the company, or by a relative of the director of such person, and any sum paid by such company in respect of any obligation but for which, such payment would have been payable by the director or other person aforesaid;

(v) Any sum chargeable to income-tax under clauses (ii) and (iii) of section 28 or section 41 or section 59;

(va) Any sum chargeable to tax u/s 28 (iiia)

(vb) Any sum chargeable to tax u/s 28 (iiib)

(vc) Any sum chargeable to tax u/s 28 (iiic)

These amendments have been made by the Finance Act 1990 in the definition of Business Profits u/s 28. The insertions given above have been introduced (a) from 1.4.62, (b) from 1.4.67 and (c) from 1.4.72.

(vd) The value of any benefit or perquisite taxable under clause (iv) of section 28;

(vi) Any capital gain taxable under section 45;

(vii) The profits and gains of any business of insurance carried on by a mutual insurance company or by a co-operative society, computed in accordance with section 44 or any surplus, taken to be such profits and gains by virtue of provisions contained in the first schedule;

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(viii) Any annuity due or commuted value or any annuity paid under the provisions of section 280 D;

(ix) Any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever.

(x) Any sum received by the assessee as his employees' contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, 1948 or any other fund for the welfare of such employees.

(xi) Any sum received under a keyman insurance policy including the sum allocated by way of bonus on such policy.

The definition of term *'Income'* as given above does not explain what income is ? It only tells that the above mentioned receipts are also included in the meaning of term *income*. The definition given u/s 2(24) is inclusive and not exhaustive. According to English dictionary, the term income means *"periodical receipts from one's business, land, work, investments etc."*

The term income simply means something which comes in. It is a periodical return with regularity or expected regularity. It's nowhere mentioned that income refers to only monetary return. It includes value of benefits and perquisites. Any thing which can reasonably and properly be described as income is taxable under this Act unless specifically exempted under the various provisions of this Act. *[Gopal Saran Narian Singh v. C.I.T. (1935) 3 I.T.R. 237, (PC)].*

The term *income* includes not only what is received by using the property but also the amount saved by using it himself. Any thing which is convertible into income can be regarded as source of accrual of income.

Features of Income. The following features of income can help a person to understand the concept of income:

(*i*) *Definite source.* Income has been compared with a fruit of a tree or a crop from the field. Fruit comes from a tree and crop from fields. Thus the source of income is definite in both cases. The existence of a source for income is somewhat essential to bring a receipt under the charge of tax.

(*ii*) *Income must come from outside.* No one can earn income from himself. There can be no income from transactions between head office and branch office. Contributions made by members for the mutual benefit and found surplus cannot be termed as income of such group.

(*iii*) *Tainted income.* Income earned legally or illegally remains income and it will be taxed according to the provisions of the Act. Assessment of illegal income of a person does not grant him immunity from the applicability of the provisions of other Act. Any expenditure incurred to earn such illegal income is allowed to be deducted out of such income only.

(*iv*) *Diversion of income vs. application of income.* Diversion of income means that a part of the income or whole of such income does not reach the

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assessee. It is diverted to some other person due to some legal obligation. Whereas the application of income means after receiving the income spending it. The amount paid by a person to his step-mother out of rent of property which he has inherited under the provisions of will from his father, is diversion of income but if there is no such provision in the will and he promises to pay some money to his step-mother, it is application of income.

(*v*) *Temporary or permanent.* Whether the income is permanent or temporary, it is immaterial from the tax point of view.

(*vi*) *Voluntary receipts.* The receipts which do not arise from the exercise of a profession or business or do not amount to remuneration and are made for reasons purely of personal nature are not included in the scope of total income.

(*vii*) *Dispute regarding the title.* In case a person is receiving some income but his title to such receipts is disputed, it will not free him from tax liability. The recipient of such income has to pay tax.

(*viii*) *Income in money or money's worth.* The income may be in cash or in kind. It is taxable in both cases.

(*ix*) Income of an assessee, *i.e.*, priest, from offerings made by the devotees from time to time has been held as income but any spontaneous offerings made out of respect, love and affection is of personal nature, hence not included in income.

Tax Treatment of Income. For the purposes of treatment of income for tax purposes it can be divided into three categories :—

A. Taxable Income. These incomes form part of total income and are fully taxable. These are treated u/s 14 to 69 of the Act. These are salaries, rent, business profits, professional gain, capital gain, interest, dividend, winnings from lotteries, races etc.

B. Exempted Incomes. These incomes do not form part of total income either fully or partially. Hence no tax is payable on such incomes. These incomes are given u/s 10(1) to 10(32) of the Act. Chapter 5 of part I of this book deals with such incomes.

C. Rebateable (Tax free) Incomes. These incomes form part of total income and are fully taxable. Tax is calculated on total income out of which a rebate of tax at average rate is allowed. The rebateable incomes given u/s 86 of the Act are :

(*i*) Share of income received by a member of an association of persons provided the total income of such AOP is assessed to tax at the rates applicable to an individual.

(*ii*) Share of income received by a partner of a firm assessed as an association of persons (PFAOP) provided the total income of such PFAOP is assessed to tax at the rates applicable to an individual.

Chapter 2 of part III of this book deals with such incomes.

9. Total Income [Section 2(45)]

'Total income' means the total amount of income referred to in section 5, computed in the manner laid down in this Act.

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10. Assessment year [Section 2(9)]

"Assessment year" means the period of 12 months commencing on the 1st day of April every year.

In India, the Govt. maintains its accounts for the period 1st April to 31st March every year. As such it is known as *financial year*. The income tax department has also selected same year for its assessment procedure.

The *Assessment year* is the financial year of the Govt. of India during which income of a person relating to the relevant previous year is assessed to tax. Every person who is liable to pay tax under this Act files return of income by prescribed dates. These returns are processed by the income tax department officials and officers. This processing is called assessment. Under this income returned by the assessee is checked and verified.

Tax is calculated and compared with the amount paid and assessment order is issued. The year in which whole of this process is undertaken is called assessment year.

At present the assessment year 1997-98 (1.4.1997 to 31.3.98) is going on.

11. Previous year [Section 3]

The term previous year is very important because it is the income earned during previous year which is to be assessed to tax in the assessment year. As the word 'Previous' means 'coming before', hence it can be simply said that the previous year is the financial year preceding the assessment year *e.g.* for assessment year 1997-98 the previous year should be the financial year ending on 31st March 1997.

(*a*) *Previous year in case of a continuing business.* It is the financial year preceding the assessment year. As such for the assessment year 1997-98, the previous year for a continuing business is 1996-97 *i.e.* 1.4.96 to 31.3.97.

(*b*) *In case of newly set up business.* The previous year in case of a newly started business shall be the period between commencement of business and 31st March next following. *e.g.* in case of a newly started business commencing its operations on Diwali 96, the previous year in relation to assessment year 1997-98. shall be the period between Diwali 96 to 31 st March 97.

(*c*) *In case of a newly created source of income.* In such case the previous year shall be the period between the day on which such source comes into existence and 31st March next following *e.g.* a person completes a new house on 1.7.96 and lets it out, the previous year for this newly created source shall be the period between 1.7.96 to 31.3.97.

Exceptions

The general rule is that the income earned during a previous year is taxed in its relevant assessment year. But there are certain exceptions to this general rule. In these cases income is taxed in the same year in which it is earned. These exceptions are:

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1. Shipping business income of non-resident ship-owners [Section 172]

In case a non-resident shipping company, which has no representative in India, earns income by carrying passengers, livestock, mail or goods loaded from any Indian port, such ship will not be allowed to leave the port till the tax on such income has been paid or alternative arrangements to pay tax are made. As such income is assessed to tax at current year's rates.

$7^1/_2\%$ of the amount received or amount receivable by the ship-owners or charters shall be deemed to be the income accruing in India on account of such carriage.

2. In cases of persons leaving India [Section 174]

In case I.T.O. has the reasons to believe that an individual will leave India with no intention to return during the current assessment year, the total income of such individual for the period between the expiry of last previous year and till the date of his departure, will be taxable in the current assessment year.

3. In case of persons who are likely to transfer their assets to avoid tax [Section 175]

If it appears to the I.T.O. that any person is likely to sell, transfer, dispose of or to part with any of his assets with the intention to avoid payment of any tax liability, he may commence proceeding to assess the income for the period between the expiry of last previous year and the date of commencement of such proceedings.

4. In case of discontinued business [Section 176]

In case any business or profession is discontinued during an assessment year, the income of the period from the expiry of last previous year till the date of discontinuation will be assessed to tax in the current assessment year.

QUESTIONS

1. Define: (*i*) Income, (*ii*) Person, and (*iii*) Assessee. [*B.Com. (Hons.), Delhi*]
2. (*a*) What is previous year? Under what circumstances income of a person can be assessed in same year in which it is earned?

   (*b*) Miss Nita, a popular singer from America came to India for the first time in her life in January 1997. She gave several performances for which she received Rs. 1,00,000. She was to board the plane on 18th March 1997 when a notice was served on her by the I.T.O. asking her to pay tax immediately. Her reply was: "My previous year is to end on 31st March 1997 and I am liable to pay tax in the assessment year 1997-98." What is your view?

   [Ans. U/s 174 she can be asked to pay tax in assessment year 1996-97 itself].
3. (*a*) Define the terms *'Previous year'* and *'Assessment year'*. What are the exceptions to the rule that income of a previous year is assessed to tax in the assessment year ? [*Mangalore University B.Com. May 1991*]

   (*b*) What will be the previous year in relation to assessment year 1997-98 in following cases :

   (*i*) A business keeping its accounts on financial year basis.

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(*ii*) A newly started business commencing its operations on 1.1.97.

(*iii*) A person giving Rs. 100,000 as loan @ 18% p.a. interest (on monthly basis) on 1.9.96.

[Hints. (*i*) 1.4.96 to 31.3.1997 (*ii*) 1.1.97 to 31.3.97
(*iii*) 1.9.96 to 31.3.97.]

4. Explain the terms (*a*) Income (*b*) Person. [*Mangalore B.Com. April 1990*]
5. Explain the concept of income and give its features.
6. Define the terms (*a*) Assessment year (*b*) Assessee.

[*Nagarjuna B.Com. March 1994*]

7. "The general rule is that the income of previous year alone should be taxed in the immediately following assessment year". Explain the exceptions to this rule ?

[*Company Secretary Inter Dec. 1993*]

Short Answer Questions

Explain the following terms in brief :

(*a*) Assessee-in-default
(*b*) Representative assessee
(*c*) Average Rate
(*d*) Fair Market value
(*e*) Charitable purpose
(*f*) Tainted Income
(*g*) Application of income
(*h*) Assessment year
(*i*) Previous year for newly set up business.

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2 AGRICULTURAL INCOME AND ITS ASSESSMENT

Need—Definition—Test—Types—Partly agricultural and partly business—Illustrations—assessment—computation of net agricultural income—calculations of tax on integration—Questions—Short Answer Questions.

NEED

Agriculture is the main part of the Indian economy. 70% of Indian population is based upon agriculture and derives its income from agricultural operations. But u/s 10(1) of the Act agricultural income is fully exempted from tax. As a result agricultural income does not form part of total income. The agricultural income is exempted from tax as under Article 270 of Indian Constitution, Central Government cannot levy any tax on such income because agriculture is a State subject. In a case *J. Ragho Rama Reddy v. I.T.O.* (1988) 169 I.T.R. 174 (A.P.) it has been held that Parliament is not competent to tax agricultural income. The State governments are free to levy any tax on agricultural income.

Due to green revolution, the agricultural incomes increased and a demand was raised to levy tax on agricultural incomes. A committee on taxation of agricultural income and wealth was set up under the chairmanship of Dr. K.N. Raj. This committee also recommended that agricultural income must remain exempted from tax. On the other hand, it suggested a system of integration of agricultural income with non-agricultural income in certain cases. From assessment year 1974-75, this scheme of assessment of agricultural income was introduced and which is known as present treatment or its assessment.

DEFINITION

The Income-tax Act, 1961 does not define what agricultural income is. Its definition is wide and inclusive. It tells us which incomes are agricultural incomes. It covers the income of cultivators and land-owners both. Under section 2(1A) of Act, *"agricultural income"* includes:

"(a) any rent or revenue derived from land which is situated in India and is used for agricultural purposes, or

(b) any income derived from such land by :

(i) agriculture; or

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(ii) the performance by a cultivator or receiver of rent-in-kind, of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him, fit to be taken to the market; or

(iii) the sale by a cultivator or receiver of rent-in-kind in respect of which no process has been performed other than a process described in the above paragraph; or

(c) any income derived from any building and occupied by the receiver of rent or revenue of such land, or occupied by the cultivator or the receiver of rent-in-kind of any land with respect of which or the produce of which any process mentioned in (ii) and (iii) above is carried on, provided the following two conditions are fulfilled:

(A) The building is situated on or in the immediate vicinity of the land and is a building which the cultivator or the receiver of rent-in-kind requires as dwelling house or as a store-house or other out-building. The house must be needed by reason of its connection with land; and

(B) The land is either assessed to land revenue in India or is subject to a local rate assessed and collected by the officers of the Govt. as such.

Where the land is not so assessed to land revenue or subject to a local rate, it must not be situated:

(i) in any area which is comprised within the jurisdiction of a municipality etc., or a cantonment board having a population of 10,000 or more as per last census; or

(ii) in any area within such distance from the local limits of municipality etc. as the Central Govt. may specify in this behalf in the Official Gazette. This distance will not exceed eight kilometers and in determining the distance, the Govt. will be guided by the extent and scope for the urbanization of that area.

From the above definition it is evident that to constitute agricultural income there must be a direct and positive link between income, land and agricultural operations. To establish this link some tests must be fulfilled, only then a particular income can be included in the definition of agricultural income.

TESTS TO DETERMINE AGRICULTURAL INCOME

The three basic tests which must be satisfied to treat a particular income as agricultural income are given below. It is essential that all the following three tests must be fulfilled :

Test (a)—Income derived from land

It is essential that for any income to be termed as agricultural income *land must be effective and immediate source of income* and not indirect and secondary. *(C.I.T. vs. Kamakshya Narain Singh).* As a result, interest on arrears of land revenue, dividend paid by a company out of its profits which included agricultural income also *(Bacha Guzdar vs. C.I.T.)* and salary paid to a manager for managing

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agricultural farms *(Premier Construction Co. Ltd. vs. C.I.T.)* are not agricultural incomes because in all these cases land is not the effective and immediate source of income.

Test (b)—Land is used to agricultural purposes

To term any income as agricultural income, it is necessary that income must be the result of agricultural operations performed on agricultural land. Agriculture means performance of some basic operations—ploughing, sowing, irrigating and harvesting and some subsequent operations—weeding, digging, pruning cutting etc. It involves employment of some human skill, labour and energy to get some income from land. *(Raja Mustafa Ali Khan vs. C.I.T.).*

Supreme Court in its decision in *[C.I.T. vs. Raja Benoy Kumar Sahas Ray (1957) 32 I.T.R. 466]* has observed:

(*i*) Agriculture in its primary sense denotes the cultivation of the field and it is restricted to the cultivation of land in strict sense of the term meaning thereby tilling of the land, sowing of seeds, planning and similar operations on the land.

(*ii*) Operations to be performed subsequently like weeding, digging etc.

(*iii*) Agriculture comprises within its scope all produce regardless of its nature. The produce may be grains, vegetables or fruits including plantations, groves and pastures, or articles of luxury such as betel, coffee, tea, spices, etc.

Test (c)—Land is situated in India

To qualify for exemption u/s 10(1) of the Act, it is necessary that agricultural income must be derived from land situated in India. In case income is derived from agricultural land situated outside India or is from any non-agricultural land, it will not be exempted u/s 10(1). It is taxable income under the head "Income from other Sources."

AGRICULTURAL INCOME—ITS TYPES

On the basis of definition of agricultural income given above, it can be classified into five broad categories. These types of agricultural incomes are:

1. Any income received as rent or revenue from agricultural land

Rent can very simply be defined as a payment in cash or in-kind which the owner of the land receives from another person in consideration of a grant of a right to use land. When the owner of land is not performing agricultural operations himself but gives his land on contract basis, any amount received from the actual cultivator by the owner of the land shall be agricultural income. Such rent may be in cash or in-kind, *i.e.,* a share in the produce grown by the cultivator.

The Privy Council decided in a case *[C.I.T. vs. Kamakshya Narian Singh (1948) I.T.R. 395]* that interest on arrears of rent payable in respect of agricultural land cannot be agricultural income, because it is neither 'rent' nor 'revenue derived from land'.

The word revenue is used in a very broad sense of return, yield or income and not only in a narrow sense of land revenue *[C.I.T. v. Kamakshya Narain Singh]*. This term embraces income other than rent and that is why mutation fees received from

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the tenants on their getting occupancy holdings and fees paid by the tenants at the time of renewal of their lease, are revenue derived from land and as such exempted from tax.

In the above mentioned case the Privy Council has clearly laid down that revenue is derived from land only if the land is immediate and effective source of the revenue and not the secondary and indirect source. So any income or revenue which is indirectly derived from land cannot be presumed to be the agricultural income. This point is further clarified by the Supreme Court in a case *Bacha Guzdar v. C.I.T.* that dividend paid by a company to its shareholders out of its agricultural income is not an income derived from land since the immediate and effective source of dividend income to the shareholder is the shareholding in the company and not the land.

Income from sale of agricultural land. The Finance Act, 1989 has added an explanation to section 2(IA) as a result of which **any revenue derived from land shall not include and shall be deemed never to have included any income arising from the transfer of any land mentioned in section 2(14) (iii) (a) or (b).** It has been made applicable retrospectively from 1.4.1970. It simply means that any income from transfer of urban agricultural land will not form part of agricultural income. It will be taxable income under the head *"Capital Gains."*

2. Income derived from Agriculture

Income derived from land situated in India by applying agricultural operations shall be agricultural income. If all the basic operations like preparation of land for sowing, planting, watering, harvesting etc. are applied, any income resulting from such operations shall be agricultural income. On the other hand, if grass, trees etc. have grown spontaneously or without the aid of human skill, effort, labour etc., any income resulting from the sale of such grass, trees or lease rent of such land shall not be agricultural income.

Agricultural income also includes income from orchards or from horticulture.

It is further to be noted that if a particular income is derived from land but without applying agricultural operations, such an income although derived from land cannot become agricultural income and so any income having remote connection with land cannot be called as agricultural income. Income from poultry and dairy farming, fisheries, mining, stone quarries, breeding and rearing of livestock, all these incomes although remotely linked with land but cannot be called agricultural incomes because of the absence of important characteristics of agricultural income, *i.e.*, cultivation of land.

Income which is in the nature of by-products of agricultural land such as selling of milk, the pasturing of cattle etc. can safely be included in agricultural income provided the endeavour is agricultural and it is reasonably connected with land used for agricultural purposes *[Beohar Singh vs. C.I.T. 16 I.T.R. 433, 443].*

3. Any income accruing to the person by the performance of any process to render the produce marketable

If, in the ordinary course, a process is to be employed by the cultivator himself or the landlord who receives the produce as rent-in-kind, any income derived from such a process shall be agricultural income. Such a process must be employed to

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render the produce fit for marketing. The process may be manual or mechanical. It should be noted that the produce should not change its original character in spite of the processing unless the produce cannot be sold in that form or condition.

Following points are to be noted in this connection:

(*a*) The process must be one which is *ordinarily employed* by the cultivator.

(*b*) The process is employed to render the produce fit to be taken to the market.

(*c*) The produce must retain its original character in spite of process unless the produce is having no market if offered for sale in its original condition.

This can further be elaborated with following examples:

(*i*) Unginned cotton can be sold in its original form and if any profit is attributable to the ginning operation, such a profit shall not be agricultural income as ginning operation is not a must to render the produce fit to be taken to the market *[Sheolal Ramlal v. C.I.T. 4 I.T.C. 375].*

(*ii*) Tabacco leaves need to be dried to make them suitable for the market and thus profit earned by selling dried tobacco shall be agricultural income. *[C.I.T. v. Katragadda Madhusudhana Rao 12 I.T.R. 1]*

(*iii*) Drying and curing of coffee after picking beans, husking of paddy, conversion of latex into sole crepe or smoked sheets. *[C.I.T. v. Woodlands State Ltd. (1965) 58 I.T.R. 612]* etc. are other examples of processes carried on to make the produce marketable.

4. Any income received by the person by the sale of produce raised or received as rent-in-kind

Any income derived by any person by the sale of agricultural produce raised by him or received as rent-in-kind shall also be agricultural income. Sometimes such person puts some extra effort by selling the produce through his own shop, any extra profit raised due to shopping activities shall not be agricultural income.

5. Income from buildings used for agriculture

Any income derived from a building used for agricultural operations shall be agricultural income provided:

(*a*) The building from where the income is received, is in the immediate vicinity of the land and is occupied by the owner, or by the cultivator or by the receiver of rent-in-kind.

(*b*) Building is used as a dwelling house or a store house or other out-building.

The cultivator or the receiver of the rent-in-kind, by reason of his connection with the land, is in need of the house as a dwelling house or as a house to store the goods required for agricultural operations.

(*c*) The land if assessed to land revenue in India or is subject to a local rate assessed and collected by officers of the Govt. and in case the land is not assessed to land revenue or to local rate, it should not be situated within the urban areas.

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PARTLY AGRICULTURAL AND PARTLY BUSINESS INCOME

Sometimes income comprises of both agricultural as well as non-agricultural income. In such a situation it becomes necessary to disintegrate such income into two parts—Agricultural income and non-agricultural income. It is for the assessee to prove that any income or part of income is agricultural income if he wants to avail the exemption u/s 10 (1) of the Act, *[C.I.T. v. Venkatswamy Naidu, 29 I.T.R. 529 (S.C.) and Bacha Gujdar v. C.I.T. 27 I.T.R. (S.C.)].*

Rule 7 of Income Tax Rules 1962

Under rule 7 the market value of the agricultural produce raised by the assessee or received as rent-in-kind and utilized as raw material, will be deducted out of the total profit of such assessee. This rule is applicable in case of cotton, tobacco, sugarcane, etc.

Market value means the price at which produce is being sold in market in its raw state. If, it is not sold in raw state, the cost of cultivation, land revenue paid or the rent of land and an element of profit as permitted by Assessing Officer, all these added together will constitute market value.

Income from manufacture of tea (Rule 8)

The income from tea plantation and tea industry is also constituted by the two elements, *i.e.*, agricultural operations carried out to grow the tea leaves and industrial operations involved in blending of tea. In such a case Income-tax Act provides that 60% of income of a tea business will be agricultural income and 40% of income will be chargeable to tax under "Profits & Gains of Business or Profession". Rule 8 applies only in case where the assessee himself grows tea leaves and manufactures tea in India.

While computing such income the cost of planting bushes in replacement of bushes that have died will be taken into consideration and an allowance shall be made.

It is for the assessee to prove whether a particular income is agricultural income or business income. He will have to satisfy the authorities in this regard.

In case any salary is received by a partner from a firm (whether assessed as PFAF or PF. A.O.P) which is engaged in the business of growing tea leaves and manufacturing tea, 60% of such salary shall be agricultural income and 40% shall be non-agricultural income.

[C.I.T. v. R.M. Chindambaram Pillai (1977) 106 ITR 292 (SC)]

Any compensation received from an insurance company or any other agency due to damage of agricultural produce caused by hail storms or other natural calamities is agricultural income. It will not be allocated into 60% or 40% ratio in case of tea business as it will be fully agricultural income.

[C.I.T. v. B. Gupta (Tea) (P) Ltd., (1969) 74 ITR 337 (Cal.)]

ILLUSTRATIONS OF AGRICULTURAL INCOMES

1. Income from the sale of trees from the forests where the trees were replanted and subsequent operations in forestry were carried out.

[C.I.T. v. Raja Benoy Kumar Sahas Roy]

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2. Income from sale of dried tobacco leaves in which green tobacco leaves are dried by using some process.

3. Amount received as compensation for dispossession of agricultural land—when an agriculturist assessee gets compensation from a person who was keeping unlawful possession of land owned by assessee as the compensation is for the agricultural income assessee would have earned.

[Commissioner of Income-tax v. Manna Bamji & Co. 86 I.T.R. 29]

4. Grazing fees realised from piece of land which was used for grazing animals used for agricultural purposes. *[C.I.T. v. Raja Shamsherjang Bahadur]*

5. Cattle are kept solely for agricultural purposes and pastured on the farm, any income from the sale of milk as well as of cream and butter made in the farm would be agricultural income.

ILLUSTRATIONS OF NON-AGRICULTURAL INCOMES

1. Incomes from sale of trees from a forest where no tilling or other basic operations were carried and trees are of spontaneous growth.

[C.I.T. v. Jyotikana Chawdhurani]

2. Income from the sale of wild grass.

3. Income derived from sale of rubber obtained by slaughter tapping of rubber trees. *[Yoosuf v. I.T.O.]*

4. Income from sale of gur or refined sugar acquired by using some manufacturing process.

5. Income from sale of ginned cotton.

6. Interest received by money-lender in the form of agricultural produce.

7. Share of agricultural produce received by a person for supply of water.

8. Remuneration received for managing agricultural farm.

[Premier Constructions Co. v. C.I.T. (1948)]

9. A Zamindar obtains promissory note from a defaulting tenant in respect of arrears of rent due to him, any interest which accrues on such note shall not be agricultural income. *[Inuganti Rajagopala Kenkata Narsimha v. I.T.O. I.T.C. 63]*

10. Commission received by the landlord for selling the agricultural produce of his tenants.

11. Profit from sale or harvest of an agricultural crop, purchased by the assessee as standing crop, may be called as profit from trading operations.

[C.I.T. v. Maddi Venkata Subbaya 20 I.T.R. 151]

12. Income from sale of *fruits* of trees of spontaneous growth is not agricultural income. *[Raja Partap Bikram Shah v. C.I.T. (1946)]*

13. Any annuity received (from agricultural land exchanged for annuity) is not agricultural income. *[Maharaj Kumar Gopal Saran Singh v. C.I.T. (1935)]*

14. Remuneration received by a person for managing agricultural property is not agricultural income. *[S.A. Ramraj v. C.A.I.T. (1969)]*

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ASSESSMENT OF AGRICULTURAL INCOME

With effect from assessment year 1974-75, the agricultural income is integrated with Non-agricultural income in certain cases of assessees. The integration is done only in those cases where assessee has both agricultural and non-agricultural incomes. In this part we have to study the computation of Net Agricultural income and rules regarding integration of agricultural income with non-agricultural income.

What to integrate ?

(*a*) *Non-agricultural Income.* It is the computed total income of assessee as per the provisions of Income-tax Act, 1961.

(*b*) *Net Agricultural Income.* It is the agricultural income computed in accordance with the rules laid down under section 2(1A) of the Income-tax Act, 1961 and rules 7 and 8 of the Income-tax Rules 1962. These rules are:

1. Rent or revenue derived from agricultural land will be computed on the same basis as adopted for computation of income under the head "income from other sources" under sections 57 to 59 of the 'Income-tax Act'.

2. Income derived from agricultural operations will be computed as if it is income chargeable to tax under the head "Profit & Gains of Business or Profession". All the provisions of sections 30, 31, 32, 34, 36, 37, 38, 40, 40A, 41, 43, and 43A of this Act shall be applicable. Depreciation and loss on the death of animals used in agricultural operations are allowed as expenses.

3. Income derived from agricultural house property will be computed as if such income is chargeable to tax under the head "Income from house property" and provisions of sections 23 to 27 shall be applicable.

4. For computing share of income from tea business income as computed under rule 8, shall be considered to be agricultural income.

5. For computing share of income or loss of a partner from the agricultural income or loss of a firm assessed as firm, same rules are applicable as are provided in Income-tax Act for computing the share of profits or losses from a firm assessed as firm.

6. Loss incurred in agriculture will be allowed to be set off only against gains from agriculture. The share of loss of partner from a firm assessed as A.O.P. *shall not* be allowed to be set off from his own agricultural income.

7. Any sum payable by the person on account of any tax levied by State Government on Agriculture will be allowed as deduction.

8. Where the net result of agricultural income from the various sources stated above in a particular previous year is loss, the loss will be disregarded and net agriculture income shall be taken to be *nil.*

When to Integrate ?

(*a*) Integration is done only in case of (i) Individuals, (ii) Hindu Undivided Families, (iii) Firms—Assessed as Association of Persons (AOP) (iv) Association of persons, (v) Bodies of individuals, and (vi) Artificial juridical persons.

(*b*) Integration is done only if Non-agricultural income of all persons mentioned above exceeds Rs. 40,000, in the relevant previous year.

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(*c*) Integration is done only if Net Agricultural income of all these persons exceeds Rs. 600 in the relevant previous year.

When not to integrate ?

(*a*) Integration is not done in case of (i) firms—assessed as firms (ii) Companies; (iii) Cooperative Societies, and (iv) Local authorities.

(*b*) No integration if Non-agricultural income of all persons mentioned earlier does not exceed Rs. 40,000, in the relevant previous year.

(*c*) No integration if the Net agricultural income does not exceed Rs. 600 in the relevant previous year.

How to integrate ?

1. Net Agricultural income is added with the Non-agricultural income if conditions given above are fulfilled.
2. Tax is calculated on this total at current rates of tax.
3. Net Agricultural income is added with the exempted limit. *i.e.* Rs. 40,000
4. Tax is calculated on this total at current rates of tax.
5. Tax calculated at point (4) is deducted out of tax calculated at point (2) above.

Balance is tax payable.

Illustration 1. Calculate the tax liability of Sh. M. Hasan for the assessment year 1997-98 :—

Net Agricultural Income	Rs. 50,000
Non-agricultural Income	Rs. 75,000

Solution : *Computation of tax liability of Sh. M. Hasan*

Assessment Year 1997-98 Rs.

1. Add Net Agricultural income with Non-Agricultural income (50,000 + 75,000) = 1,25,000)
2. Tax on Rs. 1,25,000

First	Rs. 40,000—Nil	= Nil
Next	Rs. 20,000—15%	= 3,000
Next	Rs. 60,000—30%	= 18,000
Balance	Rs. 5,000—40%	= 2,000

23,000

3. Add Net Agricultural income with exempted limit (Rs. 50,000 + Rs. 40,000 = Rs. 90,000)
4. Tax on Rs. 90,000

First	Rs. 40,000—Nil	= Nil
Next	Rs. 20,000—15%	= 3,000
Balance	Rs. 30,000—30%	= 9,000

5. Deduct tax at (4) out of tax at (2) 12,000

Balance is tax payable 11,000

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Illustration 2. Calculate tax liability of H.U.F. whose computed total income is Rs. 80,000 and Net Agricultural income is Rs. 8,000 for the assessment year 1997-98.

Solution

		Rs.
1.	Add Net Agricultural income with Non-agricultural income (Rs. 8,000 + Rs. 80,000) = Rs. 88,000	
2.	Calculate tax on this total at current rates	
	First Rs. 40,000—Nil = Nil	
	Next Rs. 20,000—15% = 3,000	
	Balance Rs. 28,000—30% = 8,400	
		11,400
3.	Add Net Agricultural Income with exempted limit *i.e.*, Rs. 40,000 (8,000 + 40,000) = 48,000	
4.	Calculate tax on this total at current rates	
	First Rs. 40,000—Nil = Nil	
	Next Rs. 8,000—15% = 1,200	
		1,200
5.	Deduct tax calculated at point (4) out of tax calculated at point (2)	
	Balance is tax payable	10,200

Illustration 3. Compute the tax liability of Mr. A. His Non-agricultural income is Rs. 1,02,000 and Net agricultural income is Rs. 50,000 for the assessment year 1997-98.

Solution

		Rs.
1.	Add Net Agricultural Income with Non-agricultural income (1,02,000 + 50,000) = 1,52,000	
2.	Calculate tax on this total	
	Tax on Rs. 1,20,000 = 21,000	
	Tax on Rs. 32,000 @ 40% = 12,800	
		33,800
3.	Add net Agricultural income with NIL rate slab (50,000 + 40,000) = Rs. 90,000	
4.	Tax on this total	
	Tax on Rs. 60,000 — = 3,000	
	Tax on Rs. 30,000 @ 30% = 9,000	
5.	Deduct tax calculated at point (4) out of tax calculated at point (2)	12,000
	Balance is tax payable	21,800

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QUESTIONS

1. Define Agricultural Income. Explain partly agriculture and partly business income. [*B.Com. Punjab*]
2. What is agricultural income ? How is it treated for income-tax purposes ? [*Mangalore B.Com. May 1991*]
3. Clearly explain the conditions to be satisfied for an income to be treated as agricultural income ? [*Nagarjuna B.Com. April 1993*]
4. How would you compute the tax liability of an individual on integration of agricultural income ?
5. Decide whether the following are agricultural incomes or not :—
   (*a*) Dividend paid by a tea company.
   (*b*) Income from interest on simple mortgage of land.
   (*c*) Salary received by a farm manager.
   (*d*) Capital gain on sale of urban agricultural land.
   (*e*) Income from cultivation and export of flowers.
   [**Hints :** (*a*) Non Agricultural Income, (*b*) Non Agricultural Income, (*c*) Non Agricultural Income, (*d*) Non Agricultural Income, (*e*) Agricultural Income]
6. Compute the tax liability for assessment year 1997-98 in each of the following cases:
   (*a*) Mr. A's total income from all other sources is Rs. 34,000 and Net Agricultural income is Rs. 1,00,000;
   (*b*) Mr. D's total income from all sources is Rs. 56,000 and Net Agricultural income is Rs. 10,000;
   (*c*) A H.U.F. has total income of Rs. 1,04,000 and Net Agricultural income of Rs. 10,000. One of the member of the family has a total income of Rs. 60,000 p.a.
   [Ans. (a) Nil, (b) Rs. 3,300, (c) Rs. 17,700]
7. Compute the tax liability of Sh. Joginder Singh for assessment year 1997-98.

		Rs.
(*a*)	Rent of Agricultural land	60,000
	Land revenue paid to State Govt.	6,000
	Interest on Loan taken to purchase agricultural land	10,000
	Collection charges on recovery of agricultural rent	1,000
(*b*)	Interest on arrears of land revenue received from tenants	12,000
(*c*)	Income from manufacturing business carried on by Mr. Singh	50,000

   [**Hint:** Agricultural Income Rs. 43,000; Non Agricultural income Rs. 62,000; Tax liability Rs. 6,600]
8. From the particulars given below compute the tax liability of Mr. Abbas for the assessment year 1997-98 :

		Rs.
(*a*)	Income from self-cultivated land (gross proceeds)	50,000
(*b*)	Rent from 10 hectares of land given to tenants (Per hectare per annum)	5,000
(*c*)	Annual rental value of the houses given to above mentioned tenants.	6,000 p.a.

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His expenses are :

1. Own cultivated land
   - (*i*) Depreciation of Equipment — 2,000 p.a.
   - (*ii*) Land Revenue paid to State Govt. — 1,200 p.a.
   - (*iii*) Purchase of seeds and fertilizers — 6,000 p.a.
   - (*iv*) Labour charges — 2,400 p.a.
2. Land given to tenants
   - (*i*) Land Revenue — 1,200 p.a.
   - (*ii*) Other expenses — 2,000 p.a.
3. House Property : Repairs — 1,200 p.a.
   - (*i*) His business profit for the year is — 52,000

[Hints : Non Agricultural Income Rs. 52,000; Agricultural Income Rs. 90,000; Tax Rs. 4,800] [P-5]

9. State with reasons whether the agricultural income is considered for income tax purposes in each of the following cases of an individual for the Assessment year 1997-98 and compute tax liability where ever necessary.

	Net Agricultural Income Rs.	Net Non-Agricultural Income Rs.	Total Rs.
1	40,000	Nil	40,000
2	500	70,000	70,500
3	10,000	28,000	38,000
4	5,000	80,000	85,000

[Karnataka B.Com. April 1995]

[Hints : 1. No integration and no tax; 2. No integration but tax payable Rs. 6,000; 3. No integration and no tax; 4. Integration and tax payable Rs. 9,750]

10. Discuss whether the following are agricultural incomes.
    - (*a*) Rent from house property situated in a village.
    - (*b*) Rent-in-kind received in respect of land given for cultivation.
    - (*c*) Life annuity received as a consideration for transfer of land used for agricultural purposes.
    - (*d*) Land leased for grazing of animals required for agricultural purpose.
    - (*e*) Income derived from land used as stone quarries.
    - (*f*) Compensation received for acquisition of agricultural land for military purposes.
    - (*g*) Income from processing of green tea leaf.
    - (*h*) Profit made by a trader in purchasing a standing crop and selling its produce.

[Bangalore B.Com. III Oct. 1995]

[Hints : (*a*) Non Agricultural income.
(*b*) Agricultural income.
(*c*) Non Agricultural income but capital receipt.
(*d*) Agricultural income.

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(*e*) Non Agricultural income.

(*f*) Non Agricultural income but capital receipt.

(*g*) If grown in own farm 60% Agricultural and 40% Business. If purchased and then processed—non-agricultural income.

(*h*) Non Agricultural income]

Short Answer Questions

Explain the following terms:

(*i*) Agricultural house property;

(*ii*) Rent from agricultural land;

(*iii*) Income from agricultural land situated outside India;

(*iv*) Income from manufacturing of tea;

(*v*) Net agricultural income;

(*vi*) Non-agricultural income;

(*vii*) Persons for whom integration of agricultural income is done;

(*viii*) Persons for whom integration of agricultural income is not done.

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3 CAPITAL AND REVENUE

Need—Capital Receipts Vs. Revenue Receipts—Immaterial Considerations—Tests of distinction—examples—Legal opinions—Capital Expenses v. Revenue Expenses—tests of distinction—Examples—Legal opinions—Capital Losses v. Revenue Losses—Illustrations—Questions.

Income tax is levied on income of assessee and not on every receipt which he receives. The method of charging tax on different types of receipts is different. Income-tax Act, 1961 provides a separate head "Capital Gains" for levying tax on capital receipts. Similarly while calculating net taxable income of an assessee only revenue expenses are allowed to be deducted out of revenue receipts. Particularly while calculating business profit or professional gain only revenue receipts and revenue expenses are considered. This makes the distinction between capital and revenue of vital importance. For this distinction capital and revenue items can be divided into three sub-parts:

CAPITAL RECEIPTS VS. REVENUE RECEIPTS

As discussed above the capital receipts are to be charged to tax under the head "Capital Gains" and revenue receipts are taxable under other heads, it is of vital importance to understand which receipt is a capital receipt and which one is a Revenue.

Immaterial Considerations

In deciding whether a particular receipt is of a capital or revenue type, the following considerations are considered to be immaterial and not going to decide or change the character or nature of the receipt.

1. *Receipt in Lump sum or in Instalments.* Whether any income is received in lump sum or in instalments, it will not make any difference as regards its nature, *e.g.*, an employee is to get a salary of Rs. 1,000 p.m. Instead of this he enters into an agreement to get a sum of Rs. 36,000 in lump sum to serve for a period of three years. The receipt where it is monthly remuneration or lump sum for 3 years is a revenue receipt. It has been decided in so many court cases that a lump sum receipt may be an item of revenue nature and an annual receipt recurring over few years may be a capital receipt. Thus, whether a receipt is a periodic receipt or a single receipt is immaterial for the purposes of determining its nature. *[Rajah Manyain Meenak and Sharma v. C.I.T. (1956) 30 I.T.R. 386].*

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2. *Nature of receipt in the hands of recipient.* Whether a receipt is capital or revenue will be determined in the hands of the persons receiving such income. No attention will be paid towards the source from which the amount is coming. Salary even paid out of capital by a new business will be a revenue receipt in the hands of employee.

3. *Magnitude of receipt.* The magnitude of the receipt, whether big or small, cannot decide the nature of the receipt although the size of a receipt in a transaction is not an entirely irrelevant consideration. A receipt of Rs. 10,000 may be of revenue nature whereas a receipt of only Rs. 1,000 may be a capital receipt. Supreme Court has ruled in a case *Divencha v. C.I.T. (48 I.T.R. 222),* that the magnitude of a receipt is immaterial for the purpose of determining its nature.

4. *Name given by parties and treatment in books of accounts.* What name the recipient or payer of the receipt has given in the books of accounts or with what name he has called a particular transaction, all such considerations are immaterial to decide the nature of the receipt. A capital payment by a dealer may be a revenue receipt in the hands of the recipient. The character of the receipt shall be decided by considerations other than by what name the parties call it. *[Divencha v. C.I.T.].* The nature of the receipt will be determined in the hands of the person receiving such income.

5. *Payment made out of capital.* No attention will be paid towards the source from which amount is coming. Salary even paid out of capital by a new business will be a revenue receipt in the hands of the employee. It was also decided in a case that if a receipt is made out of capital, the receipt may also be a capital receipt. If a recipient is beneficially entitled not only to the income but also to the capital, payments given to him by his trustees out of the corpus would be capital receipts. *[Brodie's Trustees v. I.R. 25 T.C. 13, 16].*

6. *Time of receipt.* The nature of the receipt has to be determined at the time when it is received and not afterwards when it has been appropriated by the recipient.

7. *Quality of receipt.* Whether the income is received voluntarily or under a legal obligation, it will not make any difference as regards its nature.

Distinguishing Tests

It is very difficult to draw a line of demarcation between capital receipts and revenue receipts. Even the courts have found it difficult to lay down some points of distinction on the basis of which a capital receipt may be distinguished from a revenue receipt. Some tests, however, can be applied in particular cases. These *tests* are:

1. *On the basis of nature of assets.* If a receipt is referable to fixed asset, it is capital receipt and if it is referable to circulating asset it is revenue receipt.

Fixed asset is that with the help of which owner earns profits by keeping it in his possession, *e.g.*, plant, machinery, building or factory, etc.

Circulating asset is that with the help of which owners earn profit by parting with it and letting others to become its owner, *e.g.*, stock-in-trade.

Circulating asset is asset which is turned over and while being turned over yields profit or loss whereas fixed asset is one on which the owner earns profit by keeping it in his own possession.

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Profit on the sale of motor car used in business by an assessee is capital receipt whereas the profit earned by an automobile dealer, dealing in cars, by selling a car is his revenue receipt.

2. *Termination of source of income.* Any sum received in compensation for the termination of source of income is capital receipt, *e.g.*, compensation received by an employee from its employer on termination of his services is capital receipt.

3. *Amount received in substitution of income.* Any sum received in substitution of income is revenue receipt, *e.g.*, 'A' company purchased the right to produce a film from its earlier producer with the condition that no other producer will be given these rights. Afterwards it is found that the rights for producing this film had already been sold. The 'A' company claimed damages and was awarded Rs. 40,000. It was held that damages received are the compensation for the profits which were to be earned. Hence this is revenue receipt.

4. *Compensation received on termination of lease.* Where a sum is received as compensation for termination of a lease, it is capital receipt because it is termination of source of income.

5. *Compensation on surrender of a right.* Any amount received as compensation on surrendering a right is capital receipt whereas any amount received for loss of future income is a revenue receipt. An author gives up his right to publish a book and receives Rs. 1,00,000 as compensation. It is capital receipt but if he receives it as advance royalty for 5 years it is revenue receipt.

6. *Tests as to the purpose of keeping an article.* If a person purchases a piece of sculpture to keep as decoration piece in his house, if sold later on, will bring causal receipt but if the same sculpture is sold by an art dealer it will be his revenue receipt.

If an article is acquired for the purpose of trade, the profit arising from it is revenue receipt.

Examples and Illustrations

Capital Receipts

The followings are some important examples of capital receipts decided by courts:

1. Salami or Nazrana received for grant of permanent lease.
2. Compensation received for loss of right to future remuneration.
3. Compensation received from the employer for loss of employment due to premature termination of service.
4. Price received on sale of know-how.
5. Damages received by an employee who is wrongly dismissed or a payment received by an employee in lieu of notice.
6. Amount received by the assessee for digging and removing earth from his land for brick-making.
7. Contribution received by electric supply company from consumers for installation of service lines (excess of amount over cost of installation).

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Revenue Receipts

1. Lump sum royalty received in advance.
2. A "pugree" received by the owner of the house property from tenant.
3. Damages awarded by a court to a company for breach of contract by another company.
4. A passenger is injured in a railway accident and is temporarily disabled thus losing income for a short period. Any receipt as compensation shall be a revenue receipt.

   But if the passenger is permanently disabled, the compensation received would have been a capital receipt.

SOME LEGAL OPINIONS

1. Compensation relating to stock-in-trade

A company of building contractors was refused permission by the local authority to build houses on a certain piece of land and was paid compensation. Compensation was held to be a revenue receipt as building of houses for sale was presumed to be a trading asset or stock-in-trade *[Johnson v. Try Ltd. 27 T.C. 167 C.A.]*.

2. Excess of amount recovered over actual cost

An electricity generating company collected contributions from the consumers for laying of service lines from its distributing main lines. The contributions collected exceeded the actual cost of laying the service lines. Supreme Court held that the amount so collected from the consumers is essentially the reimbursement of capital expenditure incurred by the company in laying service lines and hence the receipt including the excess recovered over the actual cost was a capital receipt. *[Hoshiarpur Electric Supply Co. v. C.I.T. 41 I.T.R. 608 and C.I.T. v. Poona Electric Supply Co. Ltd. 14 I.T.R. 622]*.

3. Compensation for restraint on trading or on exercise of profession

Such a compensation received is considered to be a capital receipt as it is in substitution of the source of income and not of only income.

A company sold its business including goodwill to another company for a certain sum. The company also entered into a covenant restraining itself from starting a similar business for 10 years for separate consideration of P.s. 10,000 p.a. It was held in a case *[C.I.T. v. Mill Store Co. 9 I.T.R. 642]* that the capital receipt had been spread over 10 years period and so the annual receipt of Rs. 10,000 was a capital receipt.

4. Compensation for breach or cancellation of contract

Compensation received for breach or cancellation of a contract, damages received for non-completion or non-execution of a contract within the stipulated time were held to be in the nature of a trading receipt.

The receipt, in the nature of damages shall be a capital receipt if it is to compensate the loss caused due to injury inflicted on the capital assets of the trade.

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Supreme Court has held in *C.I.T. v. Jai Ram Valji 25 I.T.R. 148 and C.I.T. v. South Indian Picture Ltd. 29 I.T.R. 910* that the compensation received for the termination of a contract entered into in the ordinary course of business would be a revenue receipt and on the other hand, if the agreement relates to the whole structure of the assessee's profit-making apparatus and effects the whole conduct of the business, any sum received for the cancellation or variation of such an agreement would be a capital receipt.

5. Compensation for loss of employment, agency or other office or for cessation of business

Following receipts have been held to be capital receipts. Such a compensation may be voluntary and recipient may not have any legal right to demand such a compensation :

(*i*) Compensation for cancellation of a service agreement.

(*ii*) Compensation for loss of office or employment or cessation of business.

(*iii*) Compensation for abandonment of the contractual rights of the recipient. *[C.I.T. v. Sheppard 48 I.T.R. (SC) 237].*

Compensation for loss of office on cessation of business or compensation for loss of employment are although capital receipts yet these receipts are taxable if falling under section 15 or 28(ii).

6. Compensation for requisition, acquisition, interference with business by Government

Following receipts were held to be revenue or capital receipts in a number of court cases:

Revenue Receipts

(*i*) Sum paid by the Govt. for use of requisitioned premises.

(*ii*) Compensation for loss of profits to the assessee due to controlling and interfering with assessee's right of carrying on of a business. *[C.I.T. v. Shamsher Printing Press, 39 I.T.R. 90].*

(*iii*) Compensation received in respect of stock-in-trade damaged or destroyed by enemy action.

Capital Receipts

(*i*) Compensation received for acquisition of Zamindari lands.

(*ii*) Compensation for divesting the assessee of his right to manage his business. *[Lakshmi Insurance Co. Ltd. v. C.I.T. 80 I.T.R. 575].*

(*iii*) Compensation for cancellation by the Govt. of a licence resulting in cessation of business. *[C.I.T. v. Kashmiri Mal Vasdev 39 I.T.R. 150].*

(*iv*) Compensation for requisition of business premises resulting into stoppage of assessee's business or injury to the profit-making apparatus. *[Senariam Doongarmall v. C.I.T. 42 I.T.R. 392].*

On Govt. orders, two ships ready to proceed to sea with cargo were detained in port for two days. Later on, on a suit, the Govt. had to pay compensation to the company for loss of use of ships and wages. Compensation received was held to be a revenue receipt as it was the compensation for the loss of income caused due to Govt. interruption.

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7. Nature of Subsidies or Grants received from Public Bodies

Where government gives grants or subsidies to assist a trader in his business, these are generally regarded as revenue receipts *[Meenakshi Achi. v. C.I.T. (1966) 60 I.T.R. 253 (S.C.)]*.

Where the grant or subsidy is given for a specific purpose, *e.g.*, to enable the undertaking to take steps to relieve unemployment it is not taxable as income.

8. Royalties of Writers

Royalties received by the authors of books etc. are taxable under the head 'Income from other sources' as revenue receipts.

But if there is complete assignment of copyrights, the amount of royalties or compensation received by the author shall constitute his capital receipt.

9. Recovery of an Embezzled Sum

Where an assessee had been allowed deduction regarding the amount embezzled by an employee as trading loss and subsequently it is recovered from that employee, it will form as his revenue receipt.

10. Damages for Permanent and Temporary Disability

If, in an accident, an assssee suffers a permanent disability any amount of damages received by the assessee shall be of capital nature, whereas if the injury is of a temporary nature, the amount of damages shall be a revenue receipt.

11. Refund of a Revenue Payment

Any revenue payment made to discharge a liability, if refunded later on, shall be revenue receipt when it is so refunded. For example, an assessee was allowed a deduction in respect of payment of a licence fee, it was held to be a revenue receipt when refunded in a subsequent year. *[Rahmat Ali v. C.I.T. 39 I.T.R. 505]*.

12. Lump sum Receipt or Recurrent and Periodic Income

Lump sum amount received in lieu of future royalty, single amount received in advance as ginning charges of cotton for ten years, a lump sum amount taken in communication of a right to future, commission, remuneration etc. have all been held to be revenue receipts and taxable as income, *[National Steel Works Ltd. v. C.I.T. 46 I.T.R. 646 (SC) & C.I.T. v. Harveys Ltd. 8 I.T.R. 307, 333]*.

CAPITAL EXPENSES VS. REVENUE EXPENSES

For computing profits of a business taxable under this Act, only revenue expenses are allowed to be deducted. Hence it becomes essential to distinguish a revenue expenditure from a capital expenditure. The following tests can be applied for this purpose:

(*i*) *Nature of the assets*. Any expenditure incurred to acquire a fixed asset or in connection with installation of fixed asset is capital expenditure.

Whereas

Any expenditure incurred as price of goods purchased for resale along with other necessary expenses incurred in connection with such purchase are revenue expenses.

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(*ii*) *Nature of liability.* A payment made by a person to discharge a capital liability is a capital expenditure.

Whereas

An expenditure incurred to discharge a revenue liability is revenue expenditure, *e.g.*, amount paid to a contractor for cancellation of contract to construct a factory building is capital expenditure whereas amount paid by a person—with whom he has entered into contract for supply of goods for a period of 5 years—but he fails to supply goods after 3 years, the compensation will be a revenue expenditure as it is to discharge the revenue liability.

(*iii*) *Nature of transaction.* If an expenditure is incurred to acquire a source of income, it is capital expenditure, *e.g.*, purchase of patents to produce picture tubes of T.V. sets.

Whereas

An expenditure incurred to earn an income is revenue expenditure, *e.g.*, salary of the staff, advertisement expenses, etc.

(*iv*) *Purpose of transaction.* If the amount is spent on increasing the earning capacity of an asset, it is capital expenditure, *e.g.*, expenditure incurred for fitting new windows of factory building.

Whereas

Any expenditure incurred on keeping an asset in running condition is revenue expenditure, *e.g.*, amount spent on protection of fixed assets which have already been acquired.

(*v*) *Nature of payment in the hands of payer.* If an expenditure is incurred by an assessee as a capital expenditure, it will remain as capital expenditure even if the amount may be revenue receipt in the hands of receiver, *e.g.*, purchase of motor car by a businessman is capital expenditure in his hands although it is revenue receipt in the hands of car dealer. Similarly, if the nature of payment in the hands of payer is of revenue nature, it will be a revenue expenditure even if it is capital receipt in the hands of receiver.

Capital Expenditure

1. Cost of reconstructing, refurnishing, etc. of a business building.
2. Payment made by the assessee with a view to keeping his competitor out of his field of business.
3. Expenditure incurred in converting business premises when switching over from manufacture of one product to another.
4. Expenditure on litigation in connection with acquiring or curing a defect in assessee's title to the assets of the business.
5. Compensation paid for cancellation of contract for the purchase of machinery.
6. Price paid for the purchase of partner's share in the firm.
7. Expenditure incurred on the maintenance of business reputation.

Revenue Expenditure

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1. Payments made for use of quota rights, or for use of patents and trade marks.

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2. Payment made for technical assistance and access to the fruits of continuing research *[C.I.T. v. Ciba of India Ltd. (1968) 69 I.T.R. 692 (S.C.)]*.
3. Expenditure incurred by professionals on study tour abroad to acquire latest knowledge *[Dr. Vadamalayan v. C.I.T. (1960) 40 I.T.R. 50]*.
4. Any expenditure necessary at the time of purchase to render the asset so purchased, serviceable, will be added to the initial cost as capital expenditure. But any expenditure on the replacement of part of a plant which does not bring any additional advantage to the business of assessee is revenue expenditure *[C.I.T. v. Shri Rama Sugar Mills Ltd. (1952) 91 I.T.R. 191]*.
5. Expenditure incurred to send employees abroad for practical training in the field of the business of the assessee.
6. Expenditure incurred by way of fee paid to valuer for assessing the business premises.
7. Expenditure incurred in raising loans, *e.g.*, stamp duty, registration and legal fees, brokerage etc.
8. Expenditure to oppose threatened nationalization of the industry.
9. Expenditure incurred to secure overdraft facilities from a bank.
10. Payment to the government to obtain monopoly to run buses on a route.
11. Compensation or other payment made to get rid of a servant or a managing agent in the interest of the business.
12. Any such expenditure incurred wholly, totally, necessarily for the business.

REVENUE LOSSES VS. CAPITAL LOSSES

Distinction has to be made between revenue losses and capital losses of the business because under the provisions of this Act capital losses are dealt with under the Chapter "capital gains" whereas revenue losses are treated as business losses and as such are treated under the head "Profits and gains of business or profession".

Distinction has to be made between revenue losses and capital losses of the business because under the provisions of this Act, capital losses can be set off against the income from capital gains only, whereas the revenue losses are business losses and as such can be set off against any other income of the assessee.

Ordinarily a revenue loss is one which a business sustains by sale of goods of the business or by destruction of stock-in-trade or non-recovery of any amount due from the persons who were to pay the amount.

Whereas, the capital loss is one which is related to some capital asset of the business.

It is very difficult to distinguish between a capital loss and a revenue loss on the basis of certain principles. On the basis of court judgements, following decisions have become distinguishing points:

(i) Loss due to sale of assets

Where there is loss on selling a capital asset, it is a capital loss whereas any loss incurred during the sale of stock-in-trade is a revenue loss.

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(ii) Loss due to embezzlement

Where there is embezzlement done by an employee and this causes loss to the business, it is of revenue nature.

(iii) Loss due to withdrawal of money from bank

Once the amount is deposited in bank and then it is withdrawn by an employee and is misappropiated, it is capital loss.

(iv) Loss due to liquidation of company

Amount deposited by a person with manufacturing industry to get its agency and lost due to company being liquidated is a capital loss.

(v) Loss due to theft by an employee

Loss occurring due to theft or embezzlement or misappropriation committeed by an employee is revenue loss.

Illustration 1. The following items are found debited to the Profit and Loss Account of a company. Are these items deductible in computing the income of the company for income-tax purposes? Give reasons for your answer.

(*a*) Rs. 10,000 spent on reconditioning of imperfect machinery purchased.

(*b*) Rs. 10,000 commission paid by the company for securing a contract in the course of its business.

(*c*) Rs. 20,000 bad debts written off. The bad debts were sustained by the company in respect of loans advanced to customers and written off.

(*d*) Rs. 80,000 loss on shares written off. The company has formed another company to take over its buying agency at Delhi and had taken up 80 shares of Rs. 1,000 each therein. The new company being unsuccessful, the amount of Rs. 80,000 paid on shares was lost and hence written off.

[*A.U., B.Com.*]

Solution

(*a*) The sum of Rs. 10,000 spent on reconditioning the machinery is a capital expenditure, hence it is not deductible. However, depreciation will be allowed.

(*b*) Rs. 10,000 paid as commission by the company for securing a contract in the course of its business is a revenue expenditure, hence it is deductible.

(*c*) Rs. 20.000 bad debts written off in respect of loans advanced to customers is not deductible unless the business of the company is banking or money-lending.

(*d*) Rs. 80,000 loss on investment in shares is a capital loss, hence it is not deductible.

Illustration 2. State, giving reasons, whether the following are capital or revenue receipts:

(*i*) Compensation received for compulsory vacation of place of business.

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(*ii*) Bonus shares received by a dealer of shares.

(*iii*) Money received by a Tyre Manufacturing company for sale of technical know-how regarding manufacture of tyre.

(*iv*) Dividend and interest for investments.

[*C.A. (Inter) and B.Com. (Osmania)*]

Solution

(*i*) Revenue receipt as it is in compensation of assessee's profit which it would have earned.

(*ii*) If the assessee has also converted the bonus shares into stock-in-trade then it is a revenue receipt otherwise it is an accretion in the capital asset.

(*iii*) Revenue receipt but in case the sale of technical know-how results into substantial reduction in value of the tyre company or company closes down its business in that particular line then the receipt would be a capital receipt.

(*iv*) Assessee gets the income of dividend and interest regularly and from a definite source and it is a return for the use of his asset by somebody else and so it is a revenue receipt.

Illustration 3. State whether the following are capital or revenue receipts:

(*i*) Compensation received for nationalisation.

(*ii*) Premium on issue of new shares.

(*iii*) Sales Tax collected from purchasers of goods.

(*iv*) Annuity.

(*v*) Unclaimed dividends. [*C.A. (Inter)*]

Solution

(*i*) Compensation is in substitution of assessee's source of income and hence it is a capital receipt.

(*ii*) It is not a receipt which results out of assessee's trading activities and so cannot be a revenue receipt.

(*iii*) This receipt results out of assessee's ordinary course of business and so it is a revenue receipt.

(*iv*) Annuity would be a revenue receipt if it is paid as a specified sum payable at periodical intervals. Annuity received from an employer is a salary income and in all other cases, annuity shall be chargeable under the head 'Income from other Sources'. This shall not be a taxable income in cases where the assessee exchanges his share for a capital sum payable in instalments.

(*v*) Unclaimed dividend cannot be deemed to be profit of business as dividend is neither allowed as an allowance or as deduction. It is not taxable as a receipt.

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QUESTIONS

1. What tests would you apply to distinguish capital receipts from revenue receipts? [*B.Com. Kakatiya 1992*]
2. Distinguish between Revenue Expenditure and Capital Expenditure. Give distinction between capital losses and revenue losses.
3. Distinguish between Capital and Revenue Expenditure.
4. Determine the character of the following receipts or expenditures giving reasons:
   (*i*) Sale of the assets of a firm at the time of its conversion into company for shares of equal value—part of consideration is attributable to sale of land.
   (*ii*) Profits due to fluctuation in rate of foreign currency.
   (*iii*) Money received as the consideration for not resigning directorship.
   (*iv*) Expenses incurred in connection with litigation relating to acquisition of capital assets of a business. [*G.N.D.U., B.Com.*]

   [Ans. (*i*) Capital receipt (*ii*) Capital receipt
   (*iii*) Revenue receipt (*iv*) Capital expenditure]
5. (*a*) Give the important rules regarding the distinction of capital and revenue losses for assessment purposes.
   (*b*) Explain the mode of treatment of the following:
   (*i*) An employee of a business was going to a bank to deposit some money belonging to the business. On way to the bank he lost it.
   (*ii*) The business of a person was managed by a paid manager who has power to withdraw the money from the bank account of the business. He withdrew some money and misappropriated it.
   (*iii*) Loss sustained by a business as a result of theft committed by an employee during usual working hours of the business.
   (*iv*) A cloth merchant dealing in Government securities, sold securities worth Rs. 20,000. This amount was lost by him as a result of theft committed on a railway station. [*B.Com., Punjab University*]

   [Ans. (*i*) Revenue loss (*ii*) Capital loss
   (*iii*) Revenue loss (*iv*) Capital loss, being not incidental to the business]
6. (*a*) Why is it necessary to distinguish between a capital receipt and revenue receipt? How would you determine whether a particular receipt is a capital receipt or a revenue receipt?
   (*b*) State with reasons the nature of the following:
   (*i*) A railway passenger meets with an accident and is disabled. He receives compensation from the Indian Railways.
   (*ii*) A company owning a chalk quarry contracted to supply a customer a certain quantity of chalk yearly for ten years. The purchaser after some time did not wish to take further delivery and the company agreed to release him from obligation in consideration of a lump sum payment.
   (*iii*) A company made annual payments for trucks bought under a hire-purchase agreement extending over a period of years.

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(*iv*) An assessee carried on business in several commodities. In the course of business, he submitted tenders to the railways and undertook to supply certain commodities. The amount which he had deposited as security for properly carrying out the contract was forfeited as he could not carry out the contract. [*B.Com., Punjab University*]

[**Ans.** (6b) (*i*) Capital receipt if permanently disabled and revenue receipt if disabled temporarily, (*ii*) Revenue receipt as it is in lieu of future profits, (*iii*) Capital expenditure paid in instalments, (*iv*) Revenue loss as it was in the regular course of business]

7. Why and how would you distinguish following capital receipts from a revenue receipts for income-tax purpose?

(*i*) A lump sum received by an employee from his employer as damages for termination of his services.

(*ii*) A company pays to its director a lump sum in consideration of an agreement as a result of which the later loses his right to carry on any business competing with the business of the company after his retirement.

(*iii*) A pugree received by the owner of a house from a tenant in consideration of letting his house.

(*iv*) The insurance money received, where a business concern insures its business covering its assets against loss or damage by fire and also profit caused by the stoppage of work. [*B.Com., Punjab University*]

[**Ans.** (*i*) Capital receipt, (*ii*) Capital receipt as it is surrender of right, (*iii*) Revenue receipt, (*iv*) Insurance money received against the assets is capital receipt and remaining part received against loss caused by stoppage of work is revenue receipt]

8. Determine the nature of the following transactions:

(*i*) Expenditure incurred by a bus transport organisation to oppose threatened nationalisation of bus transport business.

(*ii*) The money spent by a brewery company on publishing anti-prohibition literature.

(*iii*) Loss on the death of animals which are used for the purpose of carrying on the business of assessee.

(*iv*) A pugree (illegal premium) received by the house owner from tenant.

[**Ans.** (*i*) Revenue Expenditure, (*ii*) Revenue Expenditure, (*iii*) Revenue loss allowed under section 36 of the Act, (*iv*) Revenue receipt]

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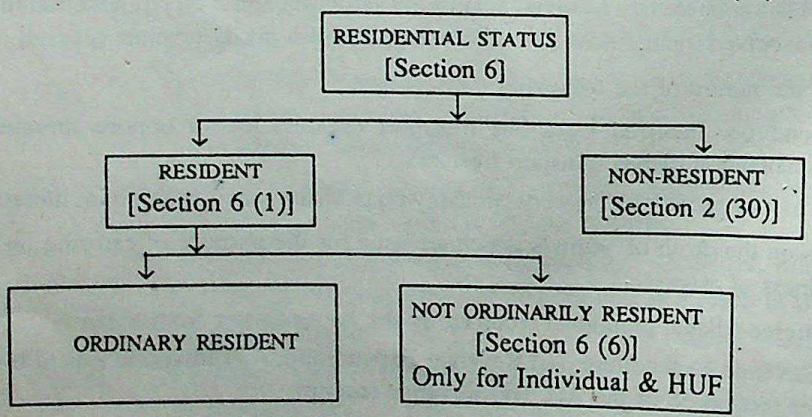
4 BASIS OF CHARGE

Need—determination of status for Individual, H.U.F., Firm, A.O.P. and Body of Individuals, company, every other Person—Incidence of tax—Total income of resident—Not ordinarily resident—Non-resident—Chart—Illustrations—Questions—Short Answer Questions.

Tax is levied on total income of assessee. Under the provisions of Income-tax Act, 1961 the total income of each person is based upon his residential status. Section 6 of the Act divides the assessable persons into three categories:

(*i*) Resident; (*ii*) Resident but Not ordinarily resident; and (*iii*) Non-Resident.



The concept of residential status has nothing to do with nationality or domicile of a person. An Indian, who is a citizen of India can be non-resident for Income-tax purposes, whereas an American who is a citizen of America can be resident of India for Income-tax purposes. Residential status of a person depends upon the territorial connections of the person with this country, *i.e.*, for how many days he has physically stayed in India.

The residential status of different types of persons is determined differently. Similarly, the residential status of the assessee is to be determined each year with reference to the "previous year". The residential status of the assessee may change from year to year. What is essential is the status during the previous year and not in the assessment year.

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I. RESIDENTIAL STATUS OF AN INDIVIDUAL

1. Resident [Section 6(1)]

To determine the residential status of an individual, section 6(1) prescribes two tests. An individual who fulfils any one of the following two tests is called Resident under the provisions of this Act. These tests are:

(a) If he is in India during the relevant previous year for a period amounting in all to 182 days or more.

Or

(b) If he was in India for a period or periods amounting in all to 365 days or more during the four years preceding the relevant previous year and he was in India for a period or periods amounting in all to 60 days or more in that relevant previous year.

Explanation—(a) In case of individual being a citizen of India who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of section 3 of the Merchant Shipping Act 1958 (44 of 1958) or for the purposes of employment outside India the provisions of sub-clause (b) as given above shall apply in relation to that year as if the words "sixty days" have been substituted by "182 days"

(b) In case of an individual being a citizen of India, or a person of Indian origin within the meaning of explanation to clause (e) of section 115 C, who being outside India, comes on a visit to India in any previous year, the provisions of sub-clause (b) shall apply in relation to that year as if for the words. 'Sixty days occurring therein the words One hundred and eighty two days had been substituted.'

From the above provisions it becomes clear that to become resident, an individual must fulfil one of the two tests given above. These tests are explained below:

Test No. 1. Stay in India for 182 days or more

If an individual is to become resident of India during any previous year, his/her personal stay in India during that year is a must although the number of days of stay differs in the two tests. It means that if an individual does not stay in India at all in any previous year, he cannot be resident of India in that year. Stay in India means that the individual should have stayed in Indian territory and anywhere (cities, villages, hills, even Indian territorial waters) for such number of days.

The period of 182 days need not be at a stretch. But physical presence for an aggregate of 182 days in the relevant previous year is enough. The status of resident is not linked with any particular place or town or house.

The onus to prove the number of days of stay in India lies on the assessee. It is for him to prove, if he desires to be taxed as non-resident or not ordinarily resident.

Test No. 2. Presence for 365 days during the four preceding previous years

A person may be frequent visitor to India. In his case, the residential status will be determined on the basis of his presence in India for 365 days in four years immediately preceding the relevant previous year. Along with this his presence for 60 days during the relevant previous year is another essential condition to be fulfilled. The purpose, object or reason of visit to and stay in India has nothing to do with the determination of residential status.

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For Indian citizen going abroad [Explanation (a)]

In case of an Indian citizen who is going outside India for a job and his contract for such employment outside India has been approved by the Central Government test (a) u/s 6(1) remains same but in test (b) *60 days* have been replaced by *182 days*.

The practical effect of this explanation is that in case of persons of Indian citizenship going abroad on a job approved by the Central Government only test (a) is to be applied during the year he is leaving India.

For Indian citizens and persons of Indian origin [Explanation (b)]

For such persons test (a) remains the same but in test (b) words '*60 days*' have been replaced to *182 days*.

The practical effect of this amendment is that those persons who are Indian citizens or persons of Indian origin living outside India and when they come to visit India only test (a) of 6 (1) is to be applied.

A person shall be deemed to be of Indian origin if he or either of his parents or any of his grand parents was born in India or undivided India [Section 115 (c) explanation to clause (c)].

2. Non-resident [Section 2(30)]

Under section 2(30) of the Income-tax Act, 1961 an assessee who does not fulfil any of the two conditions given in section 6(1)(a) or (b) would be regarded as 'Non-resident' assessee during the relevant previous year for all purposes of this Act.

3. Resident but not Ordinarily Resident [Section 6(6)]

Under section 6(6) a person is said to be "not ordinarily resident" in India in any previous year if such person is—an individual who has not been resident in India in 9 out of 10 previous years preceding that year, or has not during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, 730 days or more.

To claim this advantageous status (as compared to resident), an assessee has to prove himself as 'not ordinarily resident'. He can do so, by proving that he fulfils one of the two conditions mentioned in Section 6(6) above.

An individual can be Resident or Non-resident u/s 6(1). Once his status is determined as that of Resident—he can be either ordinary Resident or Not ordinarily resident. As every resident is ordinary resident [unless proved as Not ordinarily resident u/s 6(6)] the word ordinary is not being used.

A *resident* individual can be *not ordinarily resident* if he can prove that

(*i*) during 10 previous years preceding the relevent previous year he was *not* resident for 9 previous years. Simply it means that such resident individual should prove that he was non-resident for 2 or more previous years during 10 previous years preceding the relevent previous year.

OR

(*ii*) In case resident individual is unable to prove the test given above, he can still be regarded as *not ordinarily resident* by proving that he did not stay in India for a period or periods amounting in all to 730 days or more during seven previous

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years preceding the relevant previous year. Simply it means that he should prove that during seven previous years preceding the relevant previous year his stay in India was less than 730 days.

An individual who comes to India and is resident in a previous year remains not ordinarily resident for first 9 previous years.

Illustration 1. Mr. K, an Indian citizen leaves India for the first time on 31st May 1992 and comes back on 15th May 1995. He again leaves India on 10th June 1996 to come back on 14th January 1997. He is living in India since then. Determine his status for the previous year 1996-97.

Solution : *Determination of residential status of Mr. K.*

Relevant previous year 1.4.96 to 31.3.97

Stay in India during this year

(*i*)	1.4.96 to 9.6.96 (on 10th June he leaves India)	= 70 days
(*ii*)	14.1.97 to 31.3.97 [18 + 28 + 31]	= 77 days
	Total	147 days

Test (a) of section 6(1) is not fulfilled as his stay is less than 182 days.

Test (b) (*i*) stay during 1996-97 exceeds 60 days ; and

(*ii*) stay during 4 previous years preceding relevant previous years is

1995-96	15.5.95 to 31.3.96	=	322 days
1994-95	Not in India	=	Nil
1993-94	Not in India	=	Nil
1992-93	1.4.92 to 30.5.92	=	60 days
	Total	=	382 days

Hence he is Resident u/s 6(1) (b) but he is Not ordinarily resident u/s 6(6) as he was not resident for 9 previous years out of 10 previous years preceding the relevant previous year (being non-resident for 1993-94 and 1994-95).

Q. No. 1.

Mr. Gatting, a foreign citizen, leaves India for the first time in the last 20 years on November 25, 1994. During the calendar year 1995, he comes to India on September 1 and stays for a period of 20 days. During the calendar year 1996 he does not visit India at all but comes to India on January 15, 1997. Determine the residential status of Mr. Gatting for the assessment year 1997-98.

[**Hints** : Resident u/s 6(1) (b). Cannot be N.O.R.]

Illustration 2. Ascertain the residential status of the assessees in the following cases for the assessment year 1997-98

(*i*) Ajay is a citizen of India. He left for Iran on 18th April 1996 and could not return to India till the end of the financial year 1996-97.

(*ii*) Preetam left for U.S.A. on 10th March, 1994 after having lived in India for 20 years. He returned to India on 10th Sept. 1996.

(*iii*) Subhash is a citizen of India. He left on 15th May, 1996 for London for higher studies. He came back to India on 25 May, 1997. He maintained a dwelling place in India during his absence.

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Solution

Determination of residential status of Mr. Ajay, Preetam and Subhash for the current assessment year.

(*i*) Mr. Ajay stayed in India for 17 days during the previous year 1996-97. As he did not stay in India during that year for required number of days, so his residential status during the previous year 1996-97 shall be *non-resident.*

(*ii*) 1993-94—stayed in India for 343 days

1994-95 Nil

1995-96 Nil

1996-97—10th Sept. 1996 to 31st March 1997 = 203 days.

During the previous year, 1996-97. Pretam stayed in India for 203 days. So he satisfies the very first condition, *i.e.*, sec. 6(1)(a) and thus becomes resident. As he does not satisfy the condition of being resident in India for 9 out of 10 previous years preceding the previous year 1996-97 so his status shall be 'not ordinarily resident'.

(*iii*) During the previous year 1996-97. Mr. Subhash stayed in India for 44 days only.

He is non-resident during the previous year (1996-97) as he does not fulfil any of the two tests of Section 6(1).

Illustration 3. Mr. Rajmohan, scientist from USA was appointed as senior scientists in India on 1st April 1992. On 31st Jan. 1994 he went to Pakistan on deputation but left his family (Wife and Children) in India. On 1st May 1995 he came to India and took his family on 31st Oct. 1995. He returned to India and joined his original post on 5th Feb. 1997.

Determine the residential status of Mr. Rajmohan for the Assessment Years 1994-95 to 1997-98. *(B.Com., Mangalore April 1992)*

Solution

Determination of Residential status of Mr. Rajmohan

Assessment year 1994-95 (Previous year 1993-94)

Mr. Rajmohan was in India for 305 days during the relevant previous year. Hence he fulfils first condition given in section 6(1)(a). So, he was resident. But Mr. Rajmohan can claim the privileged status of 'Not Ordinarily Resident' because he does satisfy both the subsequent conditions given in section 6(6) as he came to India on 1st April 1992. Neither he was resident of India for 9 out of 10 years nor he was present in India for 730 days in 7 previous years preceding the relevant previous year.

Assessment year 1995-96 (Previous year 1994-95)

During the previous year, he was not in India for even one day. So his residential status during this assessment year will be that of 'non-resident'.

Assessment year 1996-97 (Previous year 1995-96)

During this previous year Mr. Rajmohan was in India for 183 days. Thus he satisfies first condition of section 6(1). As such he is resident.

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Further as he can prove both the conditions given in section 6(6) hence he will be again 'not ordinarily resident'.

Assessment year 1997-98 (Previous year 1996-97)

During this year, assessee does not satisfy any of the two conditions under section 6(1)(a) or (b). Hence he is 'non-resident'.

Q. No. 2

Mr. K.V. Rao, a senior scientist goes to Nigeria, on a job approved by Central Govt. for a period of 3 years on 15th Sept. 1996. He has never been out of India before. Determine his residential status for the previous year 1996-97.

[Hint: Non-Resident u/s 6(1)(b) explanation (b)]

II. RESIDENTIAL STATUS OF H.U.F., FIRM AND A.O.P.

To determine the residential status of these persons, above-mentioned tests cannot be applied. Section 6(2) of the act provides that status of these persons shall be determined as per tests given below:

1. Resident [Section 6(2)]

H.U.F., firm or other association of persons is said to be resident in every case except where during that year the control and management of its affairs is situated wholly outside India.

It means that if a H.U.F., firm or an association is controlled from India even partially it will be resident assessee.

The *control and management of affairs* refers to the controlling and directing power, *the head and the brain.* It means that decision making power for vital affairs is situated in India. The control and management means *de facto* control and management and not merely the right to control or manage.

In case of a firm, it is said that the control and management of firm is situated at a place where partners meet to decide the affairs of the firm. If such place is outside India, it will be said that the control and management is outside India.

2. Non-Resident [Section 2(30)]

H.U.F., firm or association of persons shall be non-resident if the control and management of affairs is situated *wholly* outside India.

3. Not Ordinarily Resident [Section 6(6) (b)]

It is only H.U.F. besides individual, which can claim the advantageous status of *Not Ordinarily Resident.* A H.U.F. will be 'Not Ordinarily Resident' if:

(*i*) its manager (Karta) has not been resident in India in nine out of ten previous years preceding the relevant accounting year; or

(*ii*) the manager had not, during the seven previous years preceding the relevant accounting year been present in India for a period or periods amounting in all to 730 days. [Section 6(6)(b)].

These two tests have to be applied in case of manager (Karta) of such H.U.F. In case the Karta has been succeeded by some other man, for computing the presence in India, the length of presence in India of each succeeding Karta will be added.

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While determining the residential status of a firm or a H.U.F. it should be noted that residential status of partners or co-parceners of a H.U.F. is of immaterial consideration. What is important to note is that from where the business is being controlled. There may be a situation where all the partners of a firm are resident in India but even then that firm may be non-resident if its full control and management lies outside India.

Illustration 4. Mr. Rabi Roy is the Karta of a H.U.F. whose property is situated in Bangladesh. During the previous year 1996-97 he came to India with his family for 15 days and went back leaving his family in India.

Solution

The residential status of this H.U.F. will be non-resident for the previous year 1996-97 as the control and management of its affairs has been wholly situated outside India.

III. RESIDENTIAL STATUS OF A COMPANY

The residential status of a company is to be determined on the basis of its incorporation or registration. Section 6(3) provides the following tests in this connection.

1. Resident [Section 6(3)]

A company is resident in India if, in relevant accounting year:

(*i*) it is an India company, or

(*ii*) during the year, control and management of its affairs is situated *wholly in India.*

2. Not Ordinarily Resident

A company cannot have this status. It can either be resident or non-resident.

3. Non-resident [Section 2(30)]

A company shall be 'non-resident' if it is not resident in India during the relevant accounting year.

It means that, a company whose control and management is situated wholly or partially outside India, will be non-resident company.

IV. RESIDENTIAL STATUS OF EVERY OTHER PERSON

Every other person includes body of individuals, a local authority and an artificial juridical person. They are either 'Resident' or "Non-Resident" but they cannot be Not ordinarily resident. [Section 6(4)].

The test to be applied is the situation of control and management. If it is situated wholly outside India, the assessee will be non-resident. If the control and management is wholly or partially situated in India, the status will be that of 'Resident'.

Some Important Rules

1. Whether an assessee is Resident or non-Resident, it is a question of fact. The onus to prove all the facts before the requisite authorities lies on the assessee.

2. An assessee cannot have different residential status for different sources of income.

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If a person is resident in India for one source of income in a particular previous year, he shall be deemed to be resident in that particular previous year in respect of all of his other sources of income. [Section 6(5)].

3. The residential status of a company would change with change in place of control and management of its affairs. A company can be resident in one year and non-resident in another.

INCIDENCE OF TAX (SCOPE OF TOTAL INCOME)

The tax is levied on total income of a person. The total income is based upon the residential status of an assessee. Section 5 provides the scope of total income which varies on the basis of status. Section 5 provides:

1. Subject to the provisions of this Act, the total income for any previous year of a person who is resident includes all incomes from whatever source derived, which,

(a) is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) accrues or arises or is deemed to accrue or arise to him in India during such year; or

(c) accrues or arises to him outside India during such year;

Provided that, in the case of a person not ordinarily resident in India within the meaning of sub-section (6) of section 6 the income which accrues or arises to him outside India shall not be included unless it is derived from business controlled in or a profession set up in India.

2. Subject to the provisions of this Act, the total income of any previous year of a person who is a non-resident includes all incomes from whatever source derived, which,

(a) is received or is deemed to be received in India in such year by or on behalf of such person; or

(b) accrues or arises or is deemed to accrue or arise to him in India.

The above provisions of section 5 can be expressed in following manner:

(i) Scope of total income of 'a Resident' [Section 5(1)]

(a) Income received or deemed to be received in India during the relevant accounting year. The place and date of accrual is immaterial.

(b) Income which accrues or arises or is deemed to accrue or arise in India during the relevant accounting year irrespective of the date and place of its receipt.

(c) Income accruing during the relevant accounting year outside India whether it is brought or not in India during the year.

(ii) Scope of total income of 'Not Ordinarily Resident' [Section 5(1)]

(a) Income received or deemed to be received in India during the relevant accounting year. The date and place of accrual is immaterial.

(b) Income which accrues or arises or is deemed to accrue or arise in India during the relevant accounting year irrespective of the date and place of its receipt.

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(*c*) Income accruing or deemed to accrue or deemed to be received outside India during the relevant accounting year from a business set up in and controlled from India.

(iii) Scope of total income of 'Non-Resident' [Section 5(2)]

(*a*) Income received or deemed to be received in India during the relevant accounting year. The date and place of accrual is immaterial.

(*b*) Income which accrues or arises or is deemed to accrue or arise in India during the relevant accounting year irrespective of the date and place of its receipt.

TYPES OF INCOMES

(*a*) **Income received in India.** Receipt of a particular income in India attracts tax liability. The essential fact is that a person must receive income in India during the relevant previous year. The income may be received by the assessee himself or by his agent, banker or broker on his behalf in India. It is not essential that a person must receive income either from business or salary. Assessee may receive income from any source.

All persons are assessable on income received in India during the relevant previous year irrespective of the residential status.

Income received in money or money's worth is taxable. Only thing essential is that it must be certain that the receipt in the form of money's worth must be income.

(*b*) **Income deemed to be received in India.** Such incomes which are not actually received by a person, but law considers them as receipt or incomes, are called incomes deemed to be received in India. The term 'Statutory receipts' can be easily used to cover this term. Following are the *instances* of incomes deemed to be received:

(*i*) Tax deducted at source is income deemed to be received by a person even though he never receives such income (u/s 198).

(*ii*) Section 7 considers the following incomes as deemed to be received by an assessee:

(*a*) Annual accretion to a recognised provident fund account of employee during the relevant previous year.

(*b*) Transferred balance of unrecognised provident fund to recognised provident fund.

(*iii*) Transfer of income without transfer of assets is deemed to be the income of transferor u/s 60 and 61.

(*iv*) Under section 8, the dividend distributed or deemed to be distributed u/s 2(22) will be deemed to be distributed in the previous year.

(*c*) **Income which 'Accrues' or 'Arises' in India.** Income can be held to accrue or arise to an assessee only when the assessee obtains a right to receive that income. No amount can be said to accrue unless it is actually due.

Accrue means "to fall as natural growth or increment, to come as an accretion or advantage" and *arise* means "to spring up, to come into existence" according to Oxford dictionary. It has been held that these two expressions—accrue and arise—

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are for all purposes synonymous. *Jiwan Dass v. Commissioner of Income Tax, Lahore. [A.I.R. (1929) LAH 609].*

Income accrues or arises at a place where the origin or source of growth of income is situated. As regards salaries, income accrues or arises in India if it is earned in India.

(*i*) Income accrues or arises to a person, who is entitled to demand and receive the income.

(*ii*) Income accrues or arises at a time or date when it ripens into a debt, *i.e.*, at that moment when assessee acquires a right to receive it.

(*iii*) In the case of salaried employees, the salary is earned in India if the person renders services in India. Income earned in India obviously arises in India.

(*iv*) In case of dealer of goods, if the purchases and sales of goods take place in India, the profits out of such sales arise in India.

(*v*) Profit from such transaction where goods are manufactured outside India but are sold in India will be split up into manufacturing profits and only mercantile profits, *i.e.*, accruing from sale transaction will be income arising in India.

(*d*) **Income deemed to Accrue or Arise in India.** Under section 9(1) of the Indian Income-tax Act, the following incomes are deemed to accrue or arise in India:

(i) Income arising from business connection in India

The term "business connection" though related with carrying on a business is totally different from it. It includes:

(*i*) maintaining a factor, agency or branch office with the object of carrying on the sale or purchase of goods or any other business.

(*ii*) forming a subsidiary company to carry on business on behalf of a parent company.

(*iii*) any financial association between the resident and non-resident.

A business connection may exist even without any regular connection.

In case of non-residents purchasing goods from India with a view to export them, any profit accruing from such transactions shall not be deemed to accrue or arise in India.

(ii) Income from any property held in India and assets or sources of income located in India

The word property includes both movable and immovable but does not include intangible assets. Intangible property like a debt is not property under the provisions of this section. A debt due to a foreigner cannot be called as asset or source of income in India, hence interest on such debt cannot be deemed to accrue or arise in India. *(C.I.T. v. Saurashtra Cement & Chemical Industries Ltd. 101 I.T.R. 502).*

In case a company carries on business in India and pays dividend out of profits made in India and taxed in India, the dividend arises directly from a source of income in India and as such dividend income of a non-resident may be deemed to accrue or arise in India. *[Calltex (India) Ltd. v. C.I.T. 21 I.T.R. 278].*

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(iii) Income from transfer of capital assets situated in India

Any gain arising from a capital asset whether movable or immovable shall be deemed to accrue in India in case the capital asset is situated in India at the time of transfer. It is immaterial that agreement is entered outside India or consideration is paid outside India.

(iv) Apportionment of profits (Explanation to section 9(i)]

In the case of a business of which all the operations are not carried in India, only that part of income shall be deemed to accrue or arise in India which is reasonably attributable to the operations carried on in India.

Where the goods are manufactured in India and were sold out side India, the profit will be apportioned in two parts—one for manufacturing operations and another for selling operations. The profits which could be reasonably attributed to selling operations will not be deemed to accrue in India. *(C.I.T. v. Ahmedbhai Umerbhai 18 I.T.R. 472).*

In cases where the income attributable to operations carried out in India cannot be ascertained, Rule 10 of Income-tax Rules 1962 provides:

(*i*) such percentage of the turnover so accruing or arising as the Assessing Officer may consider to be reasonable having regard to the facts and circumstances of the case; or

(*ii*) any amount which bears the same proportion to the total profits and gains of the business of the assessee computed in accordance with the provisions of the Act as the receipts so accruing or arising bear to the total receipts of the business; or

(*iii*) in such other manner as the Assessing Officer may deem suitable.

(v) Purchase of goods in India for export (Exp. to section 9)

In the case of non-residents, no income shall be deemed to accrue or arise in India to him through or from operations which are confined to the purchase of goods in India for the purpose of export.

No income is deemed to accrue in India to a non-resident through or from operations confined to the purchase of goods in India for export even if the purchases are made through a regular agency established in India for that purpose.

(vi) Salaries earned in India (Exp. to section 9)

This explanation provides an artificial place of accrual for income taxable under the head 'Salaries'. According to it the incomes chargeable to tax as salaries shall be deemed to accrue or arise in India if they are earned in India. The place of receipt and actual accrual of the salary is immaterial.

(vii) Salaries for Government service outside India (Exp. to section 9)

In the case of citizen of India who is employed by the Government, income chargeable under the head 'Salaries' which is payable outside India for the services rendered outside India is deemed to accrue or arise in India and hence is taxable but allowances and perquisites paid or allowed by Government outside India are exempted under section 10(7).

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(viii) Dividend paid abroad by Indian Company (Explanation to section 9)

Any dividend paid by an Indian company outside India is deemed to accrue or arise in India. A dividend declared abroad and payable abroad would not accrue in India even though the company may be Indian company but such a dividend declared by an Indian company but payable outside India would be deemed to accrue or arise in India.

(ix) Income from shooting of any picture in India (Explanation to section 9)

In the case of a non-resident, being—

1. an individual who is not a citizen of India; or
2. a firm which does not have any partner who is a citizen of India or who is resident in India; or
3. a company which does not have any shareholder who is a citizen of India or who is resident in India.

no income shall be deemed to accrue or arise in India to such individual, firm or company through or from operations which are confined to the shooting of any cinematograph film in India.

Summarised Chart

Different kinds of Incomes	*Different Types of Status*		
	Resident	*Not Ordinarily Resident*	*Non-Resident*
1. Income received or deemed to be received in India. It is immaterial whether it is earned in India or in a foreign country.	Taxable	Taxable	Taxable
2. Income earned in India whether received, paid in India or outside India.	Taxable	Taxable	Taxable
3. Income earned and received outside India from a business controlled or profession set up in India. Income may or may not be remitted to India.	Taxable	Taxable	Not
4. Income earned and received outside India from any other source (Except income under point 3).	Taxable	Not	Not
5. Income earned and received outside India in the years preceding the previous year in question and if the same is remitted to India during the current previous year.	Not	Not	Not

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Illustration 5. Which of the following incomes are taxable when the residential status of Mr. Umesh is:

(*i*) Resident, (*ii*) Not Ordinarily Resident, (*iii*) Non-Resident.

1. Income accrued in Canada but received in India Rs. 2,000.
2. Rs. 5,000 were earned in Africa and received there but brought to India.
3. Rs. 5,000 earned in India but received in Canada.
4. Rs. 10,000 earned and received in Srilanka from a business controlled from India.
5. House property income (computed) from Srilanka Rs. 2,000.
6. Rs. 4,000 was past untaxed foreign income which was brought to India during the previous year.
7. Profit earned from a business in Kanpur Rs. 10,000.

Solution: *Computation of total income of Mr. Umesh*

	Resident	*N.O.R.*	*Non-Resident*
	Rs.	*Rs.*	*Rs.*
(*i*) *Income received in India* [5(1)(a)] Income accruing in Canada but received in India	2,000	2,000	2,000
(*ii*) *Income accruing in India* [5(1)(a)] Profit from business in Kanpur.	10,000	10,000	10,000
Income earned in India but received in Canada	5,000	5,000	5,000
(*iii*) *Income accruing outside India and received outside India from a business controlled from or set up in India [5(1)(c) explanation].* Income from business in Srilanka	10,000	10,000	Nil
(*iv*) *Income accruing outside India and received outside India*			
(*a*) Income in Africa	5,000	Nil	Nil
(*b*) House Property Income in Srilanka	2,000	Nil	Nil
(*v*) Past untaxed income brought into India during relevant previous year (Exempted)	Nil	Nil	Nil
Total Income	34,000	27,000	17,000

Illustration 6. The following are the details of income of Shri Ram Lal:

1. Share of income from a firm assessed as AOP Rs. 10,000.
2. Dividend Rs. 1,000.
3. Income from Agriculture in Pakistan Rs. 20,000.
4. Salary received in India Rs. 9,800 (computed) but the services for the same were rendered in Iran.
5. Income from business (controlled from India) in Pakistan Rs. 10,000 and the income remitted to India.

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6. Income earned and received in Pakistan from bank deposits Rs. 5,000.
7. Income accrued in India but received in Iran Rs. 10,000.

Compute Mr. Ram Lal's taxable income if he is (*i*) a resident, (*ii*) a not ordinarily resident, or (*iii*) a non-resident.

Solution: *Computation of total income of Mr. Ram Lal*

	Resident Rs.	*N. O. Resident* Rs.	*Non-Resident* Rs.
(*a*) *Income received in India* [5(1)(a)]			
(*i*) Share of income in a firm assessed as an AOP	10,000	10,000	10,000
(*ii*) Dividend (gross)	1,000	1,000	1,000
(*iii*) Salary for services rendered outside India	9,800	9,800	9,800
(*b*) *Income accrued in India* [5(1)(b)]			
Income accrued in India but received in Iran	10,000	10,000	10,000
(*c*) *Income accrued & received outside India*			
Income from agricultural in Pakistan	20,000	—	—
Income from a business in Pakistan (controlled from India)	10,000	10,000	—
Bank deposits income in Pakistan	5,000	—	—
Total Income	65,800	40,800	30,800

Q. No. 3.

(*a*) Explain the incidence of tax liability.

(*b*) Mr. B, a married citizen of India left for Germany for the first time on 15.9.95 on a business trip. He returned to India on 5.6.96. During his absence from India he maintained a dwelling house for himself in Calcutta.

What will be his residential status for the assessment year 1997-98.

[*B.Com. (Pass) Delhi, Modified*]

[Ans. Resident]

Q. No. 4.

(*a*) Assessees have been divided into three categories on the basis of their residence. Explain how these categories are defined and how they affect the tax liability of an assessee.

(*b*) Mr. A an engineer, left India for London on 15th March 1996 for taking practical training in an engineering firm there. He returned to India on 28th March 1997. He was never out of India in the past.

State giving reasons what will be the residential status of Mr. A for the previous year 1996-97. [*B.Com. (Hons.) Delhi, Modified*]

[Ans. Non-Resident]

Q. No. 5

(*a*) Explain how the liability of an assessee is determined with reference to his residence. [*B.Com. (Pass) Delhi*]

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(*b*) A person after about 26 years stay in India, retired to England in April 1995 and returned to India on 15th February 1997 to take up a salaried appointment. What is his residential status for the previous year 1996-97 ?

[*P.U.B.L. 3rd Semester*]

[**Ans.** Non-Resident]

Q. No. 6

(*a*) How is residential status of an individual determined for Income-tax purposes?

(*b*) Mr. Prashant went to W. Germany for diploma course on 5th August 1996 and came back to India on 25th February 1997. His family (wife and children) remained in India. He had never been out of India before. What is his residential status for the year ending on 31st March 1997 ?

[**Ans.** Resident]

Q. No. 7

Show how the following incomes are to be assessed in the hands of an assessee who is (*a*) resident (*b*) non-resident and (*c*) not ordinarily resident.

		Rs.
(*a*)	Salary drawn during the year for employment outside India from Government of India	93,500
(*b*)	Salary drawn for employment in London office of an Indian Company for three months	18,000
(*c*)	Profits earned abroad & received in India	25,000
(*d*)	Profit earned from business transaction outside India & kept in Bank outside India	18,000
(*e*)	Dividend received from an Indian company	3,000

[**Hints.** (*a*) Resident Rs. 1,57,500, (*b*) Not ordinarily resident Rs. 1,21,500, (*c*) Non-resident Rs. 1,21,500]. [Salary accruing outside India from an Indian Co. is taxable in case of resident only].

Q. No. 8

Following are the incomes of Sri Amarnath for the financial year 1996-97 :

		Rs.
(*a*)	Interest on saving Bank deposit in Allahabad Bank, Delhi	1,200
(*b*)	Income from agriculture in Africa invested in Nepal	10,000
(*c*)	Dividend received in U.K. from an American Company, a part of which Rs. 2,000 remitted to India	10,000
(*d*)	Pension received in Belgium for services rendered in India with a Limited Company	20,000

You are required to compute his gross total income for the assessment year 1997-98 if he is a (*i*) resident (*ii*) Not ordinarily resident ; or (*iii*) Non-resident.

[*Nagarjuna Uni. B.Com. April 1992*]

[**Hints :** Limited Co. is presumed to be an Indian Co. (*a*) Resident Rs. 41,200 (*b*) N.O.R. Rs. 21,200 ; (*c*) Non-Resident Rs. 21,200].

Q. No. 9

Following are the incomes of Sri. Rathnam for the previous year 1996-97 :

		Rs.
(*i*)	Profit from the business in Bangalore	10,000
(*ii*)	Income accrued in India but received in Japan	4,000

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(*iii*)	Profit from business in Canada but received in India	5,000
(*iv*)	Income from house property in Karachi received in Bombay	4,000
(*v*)	Profit from business established in England and deposited there, the business being controlled from India	20,000
(*vi*)	Income from house property in America and deposited there	2,000
(*vii*)	Past untaxed income brought into India during the previous year	10,000

Compute the total income of Shri Ratnam for the assessment year 1997-98 if he is (a) Resident (b) N.O.R. or (c) Non-Resident.

[*Mangalore B.Com. 1988*]

[**Hints :** Resident Rs. 45,000 ; N.O.R. Rs. 43,000 and Non-Resident Rs. 23,000]

Q. No. 10

X is a foreign citizen. During the financial year 1996-97 he was in India for 101 days. Determine his residential status for the assessment year 1997-98 on the assumption that during the financial years 1982-83 to 1995-96 he was present in India as follows :

1982-83	85 days	1989-90	16 days
1983-84	310 days	1990-91	160 days
1984-85	106 days	1991-92	281 days
1985-86	174 days	1992-93	305 days
1986-87	20 days	1993-94	165 days
1987-88	280 days	1994-95	210 days
1988-89	265 days	1995-96	220 days

[*Company Secretary Inter Dec. 1993*]

[**Hints :** Resident but N.O.R]

Q. No. 11

X, an Indian citizen, is posted in the Indian High Commission at London during the previous year 1996-97. His emoluments consists of basic pay : R. 6,000 per month; and overseas allowance : Rs. 2,000 per month. Besides, he is entitled for air fare for going from and coming to India and free use of government's car at London. Is claim of X justified that since he is a non-resident during the previous year 1996-97, he is not liable to tax on salary earned and received outside India ? Does it make any difference if X is a foreign citizen ? [*Company Secretary Inter Dec. 1990*]

[**Hints :** Salary—taxable as deemed to accrue in India u/s 9 (1) but allowances and perks allowed outside India exempted u/s 10 (7)]

Q. No. 12

What is the residential status of an individual (for the assessment year 1997-98 who was in India as follows :

Previous years	Presence in India
1996-97	185 days
1995-96	15 days
1994-95	26 days

[*Company Secretary Inter Dec. 91*]

[**Hints :** Resident u/s 6 (1) (a) but N.O.R. u/s 6 (6)]

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Q. No. 13

I. During the previous year 1996-97 X, an Indian citizen, comes to India on a visit of 143 days. Determine his residential status for the assessment year 1997-98 on the basis of the following information :

(*a*) During 1992-93 X is present in India for 365 days.

(*b*) During 1991-92 and 1990-91 X is in Japan for 360 days and 345 days respectively.

(*c*) Mrs. X is a non-resident in India for the assessment year 1997-98.

II. Does it make any difference if X is an *American citizen.*

[*Company Secretary Inter June, 1993*]

[**Hints :** Case I—Non Resident, II Resident u/s 6 (1) (b) but N.O.R. u/s 6 (6)]

Q. No. 14

Head office of XY, a Hindu Undivided Family, is situated in Hongkong. The family is managed by Y who is resident in India in 7 out of 10 years preceding the previous year 1996-97. Determine the residential status of family for the assessment year 1997-98 if the affairs of the family's business are—(*a*) wholly controlled from Hongkong; and (*b*) partly controlled from India.

[*Company Secretary Inter Dec. 1992*]

[**Hints :** (*a*) H.U.F. is Non-resident (*b*) Resident but N.O.R. as Karta is N.O.R. u/s 6 (6)]

Q. No. 15

The following are the incomes of Mr. Salman for the previous year 1996-97 :

(*i*) Profit on sale of machinery in Bangalore but received in Australia Rs. 30,000.

(*ii*) Profit from business in Canada, the business being controlled from India (one-third is received in India) Rs. 42,000.

(*iii*) Income from house property in Iran Rs. 20,000.

(*iv*) Agricultural Income in England and was received there but later brought into India Rs. 8,000.

(*v*) Past untaxed foreign income brought into India during the previous year 1996-97 Rs. 6,000.

Compute the total income of Mr. Salman for the Assessment year 1997-98 if he is (*a*) Resident; (*b*) Not ordinarily resident or (*c*) Non Resident.

[*Karnataka B.Com. 1994*]

[**Hints :** Total Income if Resident Rs. 100,000, if N.O.R. Rs. 72,000 and if Non-resident Rs. 44,000]

Q. No. 16

Determine the residential status of the following assesses under the Income-tax Act for the previous year 1996-97 giving reasons for your answer :

(*a*) Mr. M.M. Agarwal came to India for the first time from Kuwait on 25th September, 1990. He stayed here for four years and left for U.K. on deputation for the Government of India on 26th September, 1994. He returned to India on 1 May, 1995 and again went to U.K. for a job offered by an English company in December, 1995. He came to India for permanent settlement on 26th September, 1996.

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(*b*) Mr. A.B Sen left India for West Germany for higher studies on 1st December, 1993. He maintained a dwelling house for him in Delhi throughout the period he was in West Germany. During winter vacations he came to India twice, once on 4th January. 1995 and stayed for 30 days and again on 25th December, 1995 and stayed for 28 days. After completing his studies he came back to India for good on 28th November, 1996.

(*c*) A Hindu Undivided Family is carrying on a family business in India. The business is having its head office in Kanpur wherefrom it is controlled. The 'Karta' of the family was in Kenya for business purposes throughout the years ended on 31 st March, 1995 and 1996.

(*d*) JKL Co. is a partnership firm registered in India and is controlled from India. Mr. J its senior partner, was in U.K. for more than 340 days during the year ended on 31st March, 1997 for business purposes.

[**Hints :** (*a*) Resident but N.O.R; (*b*) Resident but N.O.R.; (*c*) Resident but N.O.R.; (*d*) Resient] [P-6]

QUESTIONS

1 What are the different categories of assessees according to their residential status ? How would you determine the status of an individual and a firm ?
[*Mangalore B.Com. April 1993*]

2. How is residence of an assessee determined for tax purposes ? Explain the incidence of tax liability ? [*Mangalore B.Com. April 1994*]

3. When an Individual becomes Resident ? [*Kakatiya B.Com. 1992*]

4. What do you understand by the term residence of an assessee ? What conditions are laid down for determination of residence of an individual, a firm and a company ?
[*Kakatiya B.Com. (Special) 1992*]

5. How would you determine the residential status of a person ? [*B.Com. Punjab*]

6. What is the scope of total income of a person under Income tax Act 1961 ?
[*B.Com. Punjab*]

Short Answer Questions

Explain the following terms :

(*i*) Resident
(*ii*) Not ordinarily Resident
(*iii*) Residential status of a Company
(*iv*) Total income of a Resident
(*v*) Total income of a Non-Resident
(*vi*) Income deemed to be received in India
(*vii*) Salary paid to employees in India and outside India by Govt. or by private employer.

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5 EXEMPTED INCOMES

Classification of incomes—Incomes taxable under this Act—Exempted Incomes—Incomes entitled to rebate and reliefs—Exempted incomes u/s 10—Tax-free Zones—Powers of the Central Govt.

Incomes can be classified into three categories as per provisions of this Act. These categories are:

I. Incomes forming part of total income and subject to tax.

—These incomes are treated u/s 14 to 80 of the Act and have been explained in detail in Part II of this book.

II. Incomes forming part of total income but entitled to rebate or relief.

—These incomes are given u/s 86 and have been explained in Part III of this book.

III. Incomes exempted from tax.

—These incomes do not form part of total income either fully or partially.

EXEMPTED INCOMES

Section 10 of Income-tax Act has given a long list of incomes which are totally exempt from tax and so these incomes are not included in the gross total income of the assessee. In other words, such incomes are totally tax-free.

In computing the total income of any previous year of any person, any income falling within any of the following clauses shall be exempted.

1. Agriculture Income [Section 10(1)]—Fully exempted.

It has already been explained in a previous chapter.

2. Any sum received from Hindu Undivided Family (H.U.F.) [Section 10(2)]

Any sum received by an individual as a member of a Hindu Undivided Family, where such sum has been paid out of the income of the family, or in the case of any impartible estate, where such sum has been paid out of the income of the estate belonging to the family is fully exempted. This is subject to the provisions of section 64(2).

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3. Share of Income from Firm [Section 10(2A)]

In case of a person being a partner of a firm, which is separately assessed as such, his share in the total income of the firm shall be fully exempted.

The share of partner in the total income of the firm shall be in same proportion as is given in partnership deed.

4. Casual Incomes [Section 10(3)]

Casual incomes are exempted up to a total of Rs. 5,000 in a previous year. Excess, if any, is taxable under the head "Income from Other Sources".

But in case of winning from races including horse races the exemption is restricted to Rs. 2,500.

Any receipt which is of a casual and non-recurring nature and which is exempt from tax upto Rs. 5,000 [For race winnings Rs. 2,500] should satisfy the following conditions:

1. The receipt is purely casual and non-recurring.
2. The receipt is not chargeable to tax under the head 'capital gains'.
3. The receipt is not arising either from a business or the exercise, of a profession or vocation or occupation.
4. The receipt is not in the nature of additions to remuneration of an employee, *e.g.*, perquisites, bonus etc.
5. Winning from races including horse races.

Income-tax Act has not defined the words "casual" and "non-recurring" and as such these words must be understood in their plain and ordinary sense. Oxford University Dictionary has defined the term casual as (i) something produced by chance, accidental, fortuitous; (ii) coming at uncertain times, not to be calculated on, unsettled. It has been held that the following receipts are casual receipts—a gift, finding money or an article of value, a sum acquired by winning a bet, or a casual profit made upon an isolated buying and selling of some article not amounting to trade. It has been decided in number of cases *[C.I.T. v. Shamsher Printing Press, C.I.T. v. Bhaidas Cursondas]* that if a receipt is arising from a business, it shall be chargeable to tax, though it may be casual and non-recurring in nature. It has also been held in a number of court cases that a receipt which is foreseen, known, anticipated and provided for by agreement cannot be regarded as casual even if it is not likely to recur even or at least for a considerable time. *[C.I.T. v. Rao 18 I.T.R. 825. Ghanekar v. C.I.T. 80 I.T.R. 236].*

The word 'non-recurring' does not mean irregular. In Income-tax Act non-recurring receipts are those on which the assessee has no right to claim. The birthday gifts are of non-recurring nature though birthday is celebrated every year. The receipt should be both casual and non-recurring, only then it will be exempted upto Rs. 5,000. [For race winnings Rs. 2,500]

Illustration:

1. Money received by a retiring player from the sale of tickets in connection with a benefit match played for him, and
2. Money received by a person for acting as an arbitrator (he is not a professional arbitrator) are casual incomes.

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3. Tips received by a taxi-driver or a waiter in a hotel is not casual income as it is income from business or profession.
4. Gifts received by employees on Diwali will not be casual income but salary income.
5. Winning from Lotteries, winning from crossword puzzles, card games, gambling & betting etc. are all casual incomes.
6. Activity of maintenance of horses for race purposes is not casual in nature hence its income, if any, is not casual income.

5. Interest paid to Non-Resident [Section 10(4)(i)]

The amount of interest payable to a non-resident on such securities or bonds as the Central Govt. may, by notification in the Official Gazette, specify in this behalf, including income by way of premium on the redemption of such bonds, shall be exempt from tax.

6. Interest to Non-Resident on Non-Resident (External) Account [Section 10(4)(ii)]

Any income by way of interest on moneys standing to his credit in a Non-Resident (External) Account in any bank in India shall be exempt from tax in case of an individual who is a person resident outside India or is a person who has been permitted by the RBI to maintain the aforesaid account.

The person residing outside India shall have the same meaning as defined under Foreign Exchange Regulation Act, 1973, section 2(q).

7. Interest paid to a person of Indian Origin and who is Non-Resident [Section 10(4B)]

In case of an individual, being a citizen of India or a person of Indian origin, who is non-resident, any income from interest on such savings certificates issued by the Central Government, as Government may specify in this behalf by notification in the Official Gazette, shall be fully exempt.

This exemption shall be allowed only if the individual has subscribed to such certificates in Foreign Currency or other foreign exchange remitted from a country outside India in accordance with the provisions of the Foreign Exchange Act, 1973 and any rules made thereunder.

For this purpose, a person shall be deemed to be of Indian origin if he or either of parents or any of his grandparents, was born in India.

8. Travel Concession to an Indian Citizen Employee [Section 10(5)]

The provisions of section 10(5) relating to leave travel concession have been completely changed with effect from 1.4.89, *i.e.*, assessment year 1989-90 by the Direct Tax Law (Second Amendment Act 1989) which are as follows:

(*a*) Value of any travel concession or assistance received by or due to an individual from his employer for himself and his family in connection with his proceeding on leave to any place in India;

Or

(*b*) Value of any travel concession or assistance received by or due to an individual from his employer or former employer for himself and his

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family in connection with his proceeding to any place in India after retirement from service or after the termination of his service:

shall be completely exempt from tax subject to conditions given below :

1. The concession must have been allowed having regard to the travel concession or assistance granted to the Central Govt. employees.
2. In no case the exempted amount shall exceed the amount of expenses actually incurred for the purpose of this travel.
3. The term *'Family'* shall mean;
   (*a*) The spouse and children of the individual; and
   (*b*) The parents, brothers and sisters of the individual or any of them wholly or mainly dependent on the individual.

Exempted Limits are—

(*i*) *when journey is performed by rail :*
Exempted upto an amount equal to 2nd class air conditioned fare by shortest route.

(*ii*) *when journey is performed by some other mode but rail link exists :*
Exempted upto an amount equivalent to 2nd class A.C. fare by shortest route.

(*iii*) *when places are not connected by rail :*
First class or deluxe class bus fare by shortest possible route shall be exempted.

(*iv*) Leave travel concession shall be available only for two journeys performed in blocks period of 4 years commencing 1-1-89. In case such benefit is not availed in block period but is availed in first year of next block, exemption shall be allowed in such years.

(*v*) In case benefit is given without actual expenditure no exemption shall be allowed.

9. Remuneration received by a Non-resident in connection with shooting of any picture in India [Section 10(5A)]

In case of an individual who is not citizen of India and is non-resident, who comes to India mainly in connection with shooting of a picture in India, any remuneration received by him for rendering any service in connection with such shooting is fully exempt from tax.

10. Certain incomes received by technicians working with Government, local authority or scientific research institutions in India [Section 10 (5B)]

In case of an individual, who was non resident in four financial years preceding the financial year in which he arrives in India, and is rendering service as technician with the Government, local authority or statutory corporation or with any scientific research association [which is so notified u/s 10(6) (viia)], any amount of tax on his salary paid by employer to the Government shall be fully exempted u/s for a period of 48 months commencing from the date of his arrival in India.

The condition of being non-resident for four financial years may be waived by the Central Government if such technician is employed for designing, erection or commissioning of machinery or plant or in supervision of such activity. The technician should have special knowledge of manufacturing, mining, power generation, agriculture

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animal husbandry, diary farming, deep sea fishing, ship building or any other activity so notified by the Government.

11. Certain Income received by an individual who is not a citizen of India [Section 10(6)]

The following incomes are exempt when received by an individual who is not a citizen of India:

(*i*) *Passage money.* Subject to such conditions as the Central Government may prescribe, passage moneys or the value of any free or concessional passage money received by such individual from his employer or former employer for himself, his spouse and children in connection with his proceeding on leave out of India or for his home country out of India after retirement from service in India or after the termination of such service shall be exempted.

This exemption shall also be available for any amount received from employer by an employee in connection with the passage money for his children having full-time education in any educational institution outside India, while proceeding to India during vacations. [Inserted by Finance Act (2) 1977].

(*ii*) *Remuneration.* (*a*) The remuneration received by an ambassador or other officials of the Embassy, High Commission or Legation of a foreign State in India.

(*b*) The remuneration by a consular officer of a foreign State in India.

(*c*) The remuneration received by a trade commissioner or other official representative in India of a foreign State, provided corresponding officials of the Government of India in that country are given a similar concession.

(*d*) The remuneration received by a member of the staff of any of the officials referred to in (*a*), (*b*) and (*c*) above.

If the person mentioned above in (*a*) to (*d*) is a subject of the country represented, is not engaged in any business, profession or employment in India (otherwise than as a member of such staff), and the country represented gives similar concession to the members of the staff of corresponding officials of the Government of India.

(*vi*) Remuneration received by him as an employee of foreign enterprise (*e.g.*, technician deputed by a foreign firm to work in India), for service rendered by him during his stay in India provided the following conditions are fulfilled—(*a*) the foreign enterprise is not engaged in any trade or business in India; (*b*) his stay in India does not exceed in the aggregate a period of 90 days in such previous year; and (*c*) such remuneration is not liable to be deducted from the income of the employer chargeable under the Act.

(*via*) The remuneration received by him as an employee of, or a consultant to, an institution or association or a body established or formed outside India solely for philanthropic purpose, for services rendered by him in India in connection with such purposes; provided that such institution or association or body and the purposes rendered in India are approved by the Central Government. [Inserted by Taxation Laws (Amendment) Act, 1975 w.e.f. 1.10.75].

(*viia*) Remuneration received by the technician employed by the Government, local authority, corporation set up under any special law, and institution or body established in India for carrying on approved scientific research or by any business

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in India shall be exempted if the individual was not resident in India in any of the four financial years immediately preceding the financial year in which he arrived in India.

The exemption under this clause is as under:

A. *When such technician joins service before 1-4-88*

(*i*) For first 24 months from the date of his arrival in India subject to a maximum of Rs. 4,000 per month. Where the salary paid exceeds the said limit and the income-tax is payable by the employer, the tax so paid by the employer will also be exempted.

(*ii*) In case the technician continues to remain in employment in India after the expiry of 24 months with the approval of the Central Government which must be obtained before 1st October of the relevant assessment year and where the tax is paid on salary earned by the employee, the tax so paid by the employer for a period not exceeding 24 months next following the expiry of the first mentioned 24 months shall be tax-free and provisions of section 200 of Companies Act shall not be applicable.

B. *In case of technician whose services commence on or after 1-4-88 but before 1.4.1993....*

The income-tax paid by employer on salary income of such technician shall be fully exempted for a period of 48 months from the date of arrival of such technician in India.

'Technician' for the purpose of this sub-clause will mean a person who has specialised knowledge and experience in the following:

(*a*) Constructional or manufacturing operations or in mining or in the generation of electricity or any other form of power, or,

(*b*) Agriculture, animal husbandry, dairy farming, deep-sea fishing or ship-building.

The Finance Act 1979 has inserted following sub-clause in the Explanation to sub-clause (*viia*) of section 10(6):

(*c*) "Such other field as the Central Govt. may, having regard to the availability of Indians having specialised knowledge and experience therein, the needs of the country and other relevant circumstances by notification in the Official Gazette, specify."

This amendment gives power to include the technicians of any field other than given in points (*i*) and (ii) of the explanation. This amendment has come into effect from 1st June 1979.

(*viii*) *Employment on a foreign ship.* Any income chargeable under the head "Salaries" received by or due to any such individual being a non-resident, as remuneration for service rendered in connection with his *employment on a foreign ship* where his total stay in India does not exceed in the aggregate of a period of 90 days in the previous year.

(*ix*) *Remuneration received as a professor, teacher.* Any income chargeable under the head 'Salaries' received by or due to him during the thirty-six months commencing from the date of his arrival in India for services rendered as a *professor or* other teacher in a University or other educational institutional, and where any

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such individual continues to remain in employment in India after the expiry of thirty-six months aforesaid and the tax on his income chargeable under the head 'Salaries' is paid by the University or other educational institution concerned to the Central Government the tax so paid for a period not exceeding 24 months following the expiry of the 36 months aforesaid provided in either case the following conditions are fulfilled namely:

A. Such individual was not resident in any of the four financial years immediately preceding the financial year in which he arrived in India; and

B. his contract of service is approved by the Central Government:

(*a*) on or before the 1st day of October 1964, in the case of a professor or other teacher whose service commenced before the 1st day of April 1964;

(*b*) before the commencement of his service or within one year of such commencement, in any other case.

(*x*) *Remuneration received for doing research work in India.* Any sum due to or received by him, during the twenty-four months commencing from the date of his arrival in India for *undertaking any research work* in India provided the following conditions are fulfilled, namely:

(*a*) the research work is undertaken in connection with a research scheme approved in this behalf by the Central Government on or before the 1st day of October of the relevant assessment year; and

(*b*) such sum is payable or paid directly or indirectly by the Government of a foreign State or any institution or association or other body established outside India.

(*xi*) *Remuneration received by an employee of foreign govt. during his stay in India for his training in India.* Such remuneration shall be fully exempted if he is taking training in any of the following concern :

(*a*) Institution owned by govt;

(*b*) A company wholly owned by Central or State govt. or partly owned by Central and partly by State govt;

(*c*) A subsidiary Co. of company referred at point (*b*) above;

(*d*) Any corporation established by or under Central, State or Provincial Act;

(*e*) Any society registered under Societies Registration Act; 1860 and which is wholly financed by Central or State govt.

12. Tax paid by Government or Indian concern on Income of a Foreign Company [Section 10(6A), (6B) and (6C)]

(6A). Where, in the cases of foreign company, deriving income by way of royalty or fees for technical services rendered from Government or an Indian concern in pursuance of an agreement made by the foreign company with Government or Indian concern after 31.3.1976 and approved by the Government, the tax on such income is payable, under the terms of agreement by Government or such Indian concern to the Central Government—the tax so paid is fully exempted.

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With effect from 1-6-92, the Finance Act 1992 has inserted a new condition which is as follows:

"Where the agreement relates to a matter included in the industrial policy, for the time being in force, of the Government of India, such aggreement is in accordance with that policy."

(6B). Any income derived by a Non-resident non-company assessee or by a foreign company from govt. or an Indian concern under an agreement approved by Central govt., any income tax on such income payable by govt. shall be fully exempted. Such income should not be of the nature of salary, royalty or fees for technical services.

(6C). Any income derived by a foreign company (so notified by Central govt.) by way of fees for technical services under an agreement for providing services in or outside India in projects connected with security of India shall be fully exempted.

13. Perquisites and Allowances paid by Government to its Employees serving outside India [Section 10(7)]

All the perquisites and allowances paid by the Government to its employees for services rendered outside India, are exempt from tax. This exemption is allowed only to such employees of the Government who are citizens of India.

14. Employees of Foreign Countries working in India under Cooperative Technical Assistance Programme [Section 10(8)]

The persons who are working in India under co-operative technical assistance programmes in accordance with an agreement entered into by the Central Government and the Government of a foreign State, the following incomes of such individuals shall be exempt provided the terms of agreements provide for such exemption:

(*i*) the remuneration received by him directly or indirectly from the Government of the foreign State for such duties rendered in India; and

(*ii*) any other income of such individual which accrues or arises outside India and is not deemed to accrue or arise in India, in respect of which individual is required to pay any income or social security tax to the Government of that foreign State.

15. Income of a Consultant [Section 10(8A)]

Any remuneration or fee received by a consultant from an international organisation who derives its fund under technical assistance grant agreement between such organisation and the Foreign Government, and any other income accruing or arising to him outside India (which is not deemed to accrue or arise in India) and which is subject to income-tax or social security tax in foreign country, shall be fully exempted. The agreement of the service of consultant must be approved by the competent authority.

The consultant means—

(*i*) an individual who is (*a*) not a citizen of India; or (*b*) if citizen but is not ordinarily resident in India; or

(*ii*) any person who is non-resident; and is rendering technical services in India in connection with any technical assistance programme or project.

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16. Income of Employees of Consultant [Section 10(8B)]

In case of an individual who is assigned duties in India under technical assistance programme—

(*i*) the remuneration received by him directly or indirectly from any consultant as referred u/s 10 (8A) above; and

(*ii*) any other income accruing or arising to him outside India (which is not deemed to accrue or arise in India) and which is subject to income-tax or social security tax in foreign country.

shall be fully exempted provided:

(*i*) such individual is not a citizen of India; or

(*ii*) if citizen but is not ordinarily resident; and

(*iii*) the contract of service is approved by the competent authority.

17. Income of any member of the family of individuals working in India under co-operative technical assistance programmes [Section 10(9)]

The income of any member of the family of any such individual as referred to under Section 10(8) or (8A) or as the case may be clause 8(B) accompanying him to India, which accrues or arises outside India is not deemed to accrue or arise in India, in respect of which such member is required to pay any income or social security tax to the Government of that foreign State or as the case may be, country of origin of such member.

18. Gratuity [Section 10(10)]

(*i*) *Death-cum-retirement gratuity*—any such amount received by the employees working on Civil or Defence services of Govt. of India, or on any part of State Govt. or Local authority covered under Revised Pension Rules of the Central Govt. shall be fully exempted.

(*ii*) *Gratuity received under Payment of Gratuity Act*—shall be exempted upto an amount as calculated in accordance with the provisions of such Act.

(*iii*) *For other employees*—Exempted upto least of the following:

(*i*) Statutory Limit Rs. 2,50,000

(*ii*) 1/2 month's average salary for every one completed year of service;

(*iii*) Actual gratuity received.

Average salary. The Direct Tax Laws (Amendment) Act 1987 has revised the definition of average salary. In future average salary is to be calculated on the basis of average of salary received during 10 months preceding the month in which death or retirement occurs.

Statutory Limit. The present ceiling of Rs. 2,50,000 is applicable for whole service life of an employee. But with effect from assessment year 1989-90 the monetary ceiling will be such limit as the Central Government may by notification in the Official Gazette specify in this behalf keeping in view the limit applicable to Central Government employees.

Salary. The word 'salary' here has the same meaning as assigned to it for provident fund purposes, *i.e.*, the Basic Pay plus dearness pay plus any portion of D.A. which enters into pay for service benefits.

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19. Commuted value of pension received [Section 10(10A)]

(*i*) The full amount of commuted value of pension received is exempted if it is received from the Government, a local authority or a statutory corporation.

(*ii*) Any payment in commutation of pension received under any scheme from any other employer to the extent it does not exceed:

(*a*) in a case where the employee receives any gratuity, the commuted value of 1/3rd of pension which he is normally entitled to receive; and

(*b*) in any other case the commuted value of 1/2 of such pension.

20. Amount received as leave encashment on retirement [Section 10(10AA)]

(*a*) *Central & State Govt. Employees*—any payment received as the cash equivalent of the leave salary in respect of the earned leave at his credit at the time of his retirement shall be fully exempt.

(*b*) *Other employees*—any payment received as the cash equivalent of the leave salary at his credit at the time of superannuation shall be exempt upto least of the following four amounts:

(*a*) Actual amount received;

(*b*) Amount calculated at average salary of eight months (average salary means average of salary drawn by employee during 10 months immediately preceding the month of his retirement);

(*c*) Cash equivalent of leave salary due at the time of retirement.

(*d*) For persons retiring between 1-4-95 to 30-6-95 Rs. 1,30,320

For persons retiring after 30-6-95 Rs. 1,35,360

Excess of amount received over the least of the above shall be taxable.

21. Retrenchment compensation paid to workmen [Section 10(10B)]

The Finance Act, 1975 has inserted a new clause 10B in section 10 of Income-tax Act which provides that retrenchment compensation received by a workman shall be exempted from Income-tax to the extent such compensation does not exceed—

(*i*) amount calculated in accordance with the provisions of Section 15F(b) of the Industrial Disputes, Act, 1947, or

(*ii*) Rs. 50,000,

whichever is less.

This exemption will be available only to workmen as defined in Industrial Disputes Act, 1947.

With effect from 1.4.89 the monetary ceiling of Rs. 50,000 has been replaced by such amount not being less than Rs. 50,000 as the Central Govt. may, by notification in the Official Gazette, specify in this behalf. *[Direct Tax Laws Amendment Act 1987].*

22. Payment received under Bhopal Gas Leak Disaster (Processing of Claims) Act 1985 [Section 10 (10BB)]

Any amount received under the provision of such Act or any scheme framed thereunder shall be fully exempted but in case payment is received against a loss or damage, for which deduction has been claimed ealier, it shall be taxable.

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23. Retirement Compensation from a Public Sector Company or any other Company [Section 10 (10C)]

Any amount received by an employee of—

(*i*) a public sector company ; or

(*ii*) any other company ; or

(*iii*) any authority established under a Central, State or Provincial Act ; or

(*iv*) a local authority,

(*v*) a co-operative society, or

(*vi*) a university established or corporated by or under a Central, State or Provincial Act, and an institution declared to be university under section 3 of the University Grants Commission Act, 1956 ; or

(*vii*) an Indian Institute of Technology within the meaning of clause (g) of section 3 of the Institute of Technology Act, 1961 ; or

(*viii*) such institute of management as the Central Govt. may, by notification in the official gazette may specify in this behalf.

at the time of his voluntary retirement, under a scheme framed in accordance with guidelines issued by the Government and in case of companies scheme is approved by Chief Commissioner of Director General of Income-tax shall be exempted up to (*a*) Actual Amount received ; (*b*) Rs. 500,000 (*c*) 3 month's 'salary' for each completed year of service ; or, (*d*) salary last drawn multiplied by number of years' service is left ; whichever is less. In case any exemption is claimed under this clause, the employee cannot claim exemption for the same amount under any other section.

Guidelines for the above purpose [Rule 2BA of Income-tax Rules 1962]

(*i*) The scheme applies to an employee of the company who has completed 10 years of service or 40 years of age.

(*ii*) It applies to all employees except Directors of the Company.

(*iii*) The scheme has been made to result in overall reduction in the existing strength of the employees of the Company.

(*iv*) The vacancy so caused is not to be filled up and retired employee is not to be employed again in another company or concern belonging to the same management.

(*v*) The amount payable is to be calculated as 3 months salary for each completed year of service, or salary at the time of retirement multiplied by the balance months of service left before his date of retirement or superannuation.

(*vi*) The employee should not have availed benefit of any other voluntary retirement scheme earlier.

(*vii*) The term '*Salary*' shall have the same meanings as it has for provident fund purposes.

24. Any sum received under a life insurance policy [Section 10(10D)]

Any sum received under a life insurance policy, including the sum allocated by way of bonus an such policy. This provision shall not be applicable on any sum received u/s 80 DDA (3).

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25. Payment from Statutory Provident Fund [Section 10(11)]

Any amount withdrawn from the statutory provident fund is exempt from tax. This provision is applicable on Public Provident Fund also.

26. Payment from Recognised Fund [Section 10(12)]

The accumulated balance due and becoming payable to an employee participating in a recognised provident fund, is exempt to the extent provided in rule 8 of part A of the Fourth Schedule.

27. Payment from Superannuation Fund [Section 10(13)]

Any payment from an approved superannuation fund made—

(*i*) on the death of a beneficiary; or

(*ii*) to an employee in lieu of or in commutation of an annuity on his retirement at or after a specified age or on his becoming incapacitated prior to such retirement; or

(*iii*) by way of refund of contribution on the death of beneficiary; or

(*iv*) by way of refund of contribution to an employee on his leaving the service in connection with which the fund is established otherwise than by retirement age or after a specified age or on his becoming incapacitated prior to such retirement, to the extent to which such payment does exceed the contributions made prior to the commencement of this Act and any interest thereon.

28. House Rent Allowance [Section 10(13A) Read with Rule 2A]

(*a*) *Persons living in rented houses*

Any amount of House Rent Allowance received by the employee from his employer is exempted up to the least of the following limits:

(*i*) excess of actual rent paid over 10% of salary;

(*ii*) an amount equal to 50% of salary where such accommodation is situated in any one of the following places, namely, Bombay, Calcutta, Delhi and Madras and 40% of salary in other towns; or

(*iii*) actual amount of House Rent Allowance received.

(*b*) *Persons living in their own houses or not paying any rent but getting HRA*— Full HRA received is taxable. No exemption under this provision. [Inserted by Taxation Laws (Amendment) Act 1984 w.e.f. from 1.4.76].

29. Any Allowance given for meeting Business Expenditure [Section 10(14)]

Any such special allowance or benefit, not being in the nature of a perquisite within the meaning of clause (2) of section 17 specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, as the Central Government may, by notification in the Official Gazette, specify, to the extent to which such expenses are actually incurred for that purpose.

(*i*) any such allowance granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at place where he ordinarily resides, or to compensate

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him for the increased cost of living, as the Central Government may, by notification in the Official Gazette, specify, to the extent specified in the notification.

(*ii*) With effect from 1.4.89, *i.e.*, assessment year 1989-90, the Direct Tax Laws (Second Amendment) Act 1989 has inserted the following proviso:

Nothing given in sub-clause (ii) shall apply to any allowance in the nature of personal allowance granted to the assessee to remunerate or compensate him for performing duties of special nature relating to his office or employment unless such allowance is related to the place of his posting or residence.

30. Income from Exchange Risk Premium [Section 10(14A)]

Any income received by a Public Financial Institution as exchange risk premium from any person borrowing foreign currency from such institution shall be exempted provided the amount of such premium is credited by such institution to a fund specified under section 10(23E).

31. Interest Incomes [Section 10(15)]

The following interest incomes due to an assessee are exempt from tax:

(*i*) (*a*) Income by way of interest, premium on redemption or other payments on such securities, bonds, annuity certificates, savings certificates, other certificates issued by the Central Government shall be exempted if such notification is issued by Central Government in Official Gazette and shall be subject to such conditions and limits as prescribed in such notification.

(*ii*) In the case of an individual or a H.U.F. interest on such Relief Bonds as the Central Government may, by notification in the Official Gazette, specify in this behalf.

(*ii*) (*b*) Interest on such Capital Investment Bonds held by individual or H.U.F. and so notified.

(*iii*) Interest on securities held by the Issue Dept. of the Central Bank of Ceylon, constituted under the Ceylon Monetary Law Act, 1949.

(*iii*) (*a*) Interest payable to any bank incorporated in a country outside India and authorised to perform Central Banking functions in that country on any deposit made by it, with the approval of the Reserve Bank of India, with any Scheduled Bank.

(*iv*) Interest payable—

(*a*) by Government or a local authority on money borrowed by it from sources outside India;

(*b*) by an industrial undertaking in India on money borrowed by it from such financial institution in a foreign country as is approved in this behalf by the Central Government;

(*c*) by an industrial undertaking in India on any moneys borrowed or debt incurred in a foreign country in respect of its purchase outside India of raw materials or components, plant or machinery, to the extent of amount calculated at the rate approved by the Central Government in this behalf;

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(*d*) by the Industrial Finance Corporation of India established by the Industrial Finance Corporation Act, 1948 or the Industrial Development Bank of India established under the Industrial Development Bank of India Act, 1964 or Export Import Bank of India, or the National Housing Bank; or the Small Industries Development Bank of India; or the Industrial Credit and Investment Corporation of India (a company formed and registered under the Indian Companies Act, 1956) on any moneys borrowed by it from sources outside India, to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf, having regard to the terms of the loan and its repayment;

(*e*) by any other financial institution established in India or a banking company to which the Banking Regulation Act, 1940 applies (including bank or banking institution referred to in Section 51 of that Act), on any moneys borrowed by it from sources outside India under a loan agreement approved by the Central Government where the moneys are borrowed either for the purpose of advancing loans to industrial undertakings in India for purchase outside India of raw materials or capital plant and machinery or for the purpose of importing any goods which the Central Government may consider necessary to import in the public interest to the extent to which such interest does not exceed the amount of interest calculated at the rate approved by the Central Government in this behalf, having regard to the terms of the loan and its repayment;

(*f*) by an industrial undertaking in India on any moneys borrowed by it in foreign currency from sources outside India under approved loan agreement. The loan agreement is to be approved by the Central Government of India. The exempted rate of interest is also to be fixed by the Central Government having regard to the terms of the loan and its repayment; For the purposes of this sub-clause, the expression "Industrial undertaking" means any undertaking which is engaged in—

(*a*) the manufacture or processing of goods; or

(*b*) the business of generation or distribution of electricity or any other form of power; or

With the effect from assessment year 1998-99 clause (ba) has been inserted : (ba) the business of providing telecommunication services ;

(*c*) mining; or

(*d*) the construction of ships; or

(*e*) the operation of ships or aircrafts or construction or operation of rail systems.

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(*fa*) by a schedule bank, on deposits in foreign currency where the acceptance of such deposits by the bank is approved by Reserve Bank of India.

(*g*) by a public company whose main object is of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential houses, on any money borrowed by it in foreign currency from outside India upto the rate prescribed by Govt.

(*h*) by any public sector company in respect of such bonds or debentures. The holder of such bonds or debentures must register his name and the holding with that company.

(*i*) by Government on deposits made by an employee of the Central Government or a State Government in accordance with such scheme as the Central Govt. may frame and notify in Official Gazette, out of moneys due to him on account of his retirement whether on superannuation or otherwise.

(*v*) Interest on securities held by the Welfare Commissioner Bhopal gas victims Bhopal is the Reserve Bank's SGL— A/C No. SL/DHO48 shall be fully exempted. Interest on any deposits (so notified) held for the benefit of victims of Bhopal gas tragedy held with Reserve Bank of India or any Public Sector Bank shall be fully exempted.

32. *Payment made by an Indian Company engaged in the business of operation of aircraft* [Section 10(15A)]

Such payment made to acquire an aircraft or an aircraft engine on lease (other than for providing spares, facilities or service in connection with this operation of leased aircraft) to foreign govt. or a foreign enterprise under an agreement approved by Central govt. shall be fully exempted.

This clause is being omitted with effect from assessment year 1998-99.

33. *Scholarship* [Section 10(16)]

The full amount of scholarship granted to meet the cost of education is exempted.

34. *Allowance of M.P./M.L.A./or M.L.C.* [Section 10(17)]

Any income by way of

(*i*) Daily allowance received by M.P./M.L.A. or M.L.C. or any committee thereof is fully exempted.

(*ii*) any allowance received by any person by reason of his membership of Parliament under the Members of Parliament (Constituency Allowance) Rules, 1986 is fully exempted.

(*iii*) all other allowances received by any person by reason of his membership of any State Legislature or of any Committee thereof, which the Central Government may notify, shall be exempted upto Rs. 600 p.m. only. Excess shall be taxable.

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Limit of Rs. 600 pm is being raised to Rs. 2,000 pm with effect from assessment year 1998-99.

35. Awards Instituted by Govt. [Section 10(17A)]

(*i*) Any payment made whether in cash or in kind under any awards instituted in the public interest by the Central or State Government or instituted by any other body and approved by the Central Govt. in this behalf shall be fully exempted.

(*ii*) Any other reward given by Central or State Government for such purposes as may be approved by the Central Government in this behalf in public interest shall also be fully exempted.

36. Exemption in some cases to ex-rulers of Indian States [Section 10 (18A, 19A)]

Under Section 18A, any ex-gratia payments given to the ex-rulers of Indian States consequent on the abolition of privy purses is exempt.

Annual value of any palace in the occupation of former rulers of Indian states shall be fully exempted.

37. Income of a local authority [Section 10(20)]

The following types of incomes in the hands of a local authority are exempt from tax—

(*i*) Income from house property,

(*ii*) Capital gains,

(*iii*) Income from other sources, or

(*iv*) From a trade or business carried on by it which accrues or arises from the supply of a commodity or service (not being water or electricity) within its jurisdictional area or from the supply of water or electricity within or outside its own jurisdictional area.

38. Income of a Housing Authority or Housing Boards [Section 10(20A)]

Any income of authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfy the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages or for both.

39. Income of scientific research association [Section 10(21)]

Any income of an approved scientific research association and if the same income is applied solely for the purposes of that association, *i.e.*, for carrying scientific research.

40. Income of a university or other educational institutions [Section 10(22)]

Income of a university or any other educational institution which is set up solely for educational purposes and not for purposes of profit.

If an educational institution solely running for educational purposes earns some income incidentally, *e.g.*, from compilation, publication, printing and selling of text-

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books and profits from such activities are to be used only for development, expansion and spread of education, such an income shall also be exempted from tax.

[Secondary Board of Education v. I.T.O. 86 I.T.R. 408 (Orissa)]

41. Income of Hospitals, etc. [Section 10(22A)]

Income of hospitals and such other medical institutions which are existing solely for philanthropic purposes and not for profit making purposes.

42. Income of a News Agency [Section 10(22B)]

In case there is any income of a news agency set up solely in India for collection and distribution of news and which is so notified in this behalf shall be fully exempted provided such income or accumulated income is used solely for collection and distribution of news and not to be distributed in any manner amongst its members.

43. Income of Sports Associations [Section 10(23)]

The income of all such sports bodies which are set up for the purposes of control, supervising, regulation and encouragement of sports in India. All such sports associations are to satisfy the following conditions:

(*i*) The association or institution applies its income or accumulates it for application, solely to the objects for which it is established.

(*ii*) No part of the income of the association or institution is distributed in any manner to its members except to any association or institution affiliated to it.

(*iii*) The association or institution is, for the time being approved for the purpose of this clause by the Central Government by general or special order.

44. Income of some Professional Institutions [Section 10(23A)]

Any income other than income chargeable under the head 'income from house property or any income received for rendering any specific services or income by way of interest or dividends derived from its investments of an association or institution established in India having its object as the control, supervision, or encouragement of the profession of law, medicine, accountancy, engineering or architecture or such other profession as the Central Government may notify in the Official Gazette. The following conditions are to be satisfied before any exemption is allowed under this clause:

(*i*) The association or institution applies its income or accumulates it for application, solely to the objects for which it is established.

(*ii*) The institution or association is approved for the purpose by the Central Government.

45. Exemption of Income Received by Regimental Fund [Section 23 AA]

Any income received by any person on behalf of any Regimental Fund or Non Public Fund established by the armed forces of India for the welfare of the past and present members of such forces or their dependents shall be exempted from tax.

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46. Income of a Fund set-up for the welfare of employees or their dependents [Section 10(23AAA)]

Any income of such fund which is approved by Commissioner of Income-tax shall be fully exempted provided its income is applied wholly and exclusively for this objects for which it is established.

47. Income of a pension fund set up by LIC [Section 10(23AAB)]

Any income of a fund set up by Life Insurance Corporation of India on or after 1.8.1996 under a pension scheme shall be fully exempted if contribution to such fund is made by any person for receiving pension from such fund which is approved by the Controller of Insurance.

48. Income of Institutions established for development of Khadi and Village Industries [Section 10(23B)]

From the assessment year 1975-76, the public charitable trusts and societies registered under the Societies Registration Act, 1860 will be entitled to claim exemption from Income-tax for the income derived by such institutions from the production, sale or marketing of Khadi or products of village industries. The exemption will not be allowed unless the institution applies its income or accumulates it for application solely for the development of Khadi or Village Industries. Only such institutions will qualify for exemption which are approved by Khadi or Village Industries Commission.

49. Income of State Level Khadi and Village Industries Board [Section 10(23BB)]

Any income from an authority (whether known as the Khadi and Village Industries Board, or by any other name) established in a State by or under a State or Provincial Act for the development of Khadi or Village Industries in the State, shall be exempted from tax.

50. Income of certain Authorities set up to manage Religious and Charitable institutions [Section 10(23BBA)]

Any income of any body or authority established, or appointed by or under any Central, State or Provincial Act which provides administration of any of the following institutions:

(*a*) Public, Religious or Charitable Trusts;

(*b*) Endowments (including Maths, Gurudwaras, Temples, Wakfs etc.); or

(*c*) a society for religious or charitable purposes registered under Societies Act 1860, shall be exempted from tax.

51. Income of European Economic Community [Section 10(23BBB)]

Any income of European Economic community derived in India by way of interest, dividend or capital gain from investments made out of its funds under such scheme as the Central Govt. may notify is fully exempted.

52. Income of a SAARC Fund for regional projects [Section 10(23BBC)]

Any income of a fund set up as SAARC Fund for Regional Projects set up by Colombo Declaration issued on 21st Dec. 1991 by Heads of State or Government of the

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Member Countries of South Asian Association for Regional Co-operation shall be fully exempted.

53. Any income received by a person on behalf of following Funds [Section 10(23C)]

Any income received by any person on behalf of—

(*i*) the Prime Minister's National Relief Fund; or
(*ii*) the Prime Minister's Fund (Promotion of Folk Art); or
(*iii*) the Prime Minister's Aid to Student's Fund; or
(*iv*) any other fund established for charitable purposes which may be notified by Central Government; or
(*v*) any trust or institution set up wholly for religious purposes or purpose which may be notified by the Central Government.

The above exemption shall not be available for the profits and gains of any business which is carried on, on behalf of or by any fund or institution referred in points (*iv*) and (*v*) above or to the profits or gains of any business undertaking held under trust for the purposes of any fund or institution referred in points (*iv*) and (*v*) above. This amendment has come into effect from assessment year 1984-85.

54. Income from Mutual Fund [Section 10(23D)]

Any income of such Mutual Fund set up by a public sector bank or a public financial institution or any fund authorised by Securities & Exchange Board of India or Reserve Bank of India and subject to such conditions as the Central Govt. may, by notification in the Official Gazette, specify in this behalf.

'Public Sector Bank' means the State Bank of India, all its subsidiary banks and all other nationalised banks. The expression 'public financial institution' shall have the meaning assigned to it in Section 4A of the Companies Act, 1956.

55. Income of Exchange Risk Administration Fund [Section 10(23E)]

In case such fund is set up by Public financial institutions either jointly or separately and is notified in Official Gazette by Central Government, any income from such fund shall be fully exempted.

In case any amount standing to the credit of the Fund and has been claimed to be exempted during any previous year, is shared wholly or partly with a public financial institution, the whole of amount so shared shall be deemed to be income of the previous year in which such amount is so shared and shall be assessable to tax accordingly.

56. Income of Venture Capital Company [Section 10 (23F)]

Income by way of dividend or long-term capital gains of a Venture Capital Fund or Venture Capital Company from investments made by way of equity shares in a Venture Capital undertaking shall be fully exempted.

57. Income by way of dividend, interest or long term capital gains of an infrastructure capital company [Section 10(23G)]

Any income derived by a infrastructure capital company by way of dividends, interest or long term capital gains from any investment made in enterprise carrying

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on the business of developing, maintaining and operating infrastructure facility which fulfills the conditions specified in 80IA(4A) shall be fully exempted.

The term infrastructure capital company means a company which has been made investments by way of acquiring shares or providing long-term finance to an enterprise carrying on the business of developing, maintaining and operating infrastructure facility.

The term infrastructure facility shall have same meaning as is given u/s 80(IA)(12).

The term long-term finance shall have same meaning as is given u/s 36(1).

With effect from assessment year 1998-99 the meaning of infrastructure facility will be :

(*i*) a road, highway, bridge, airport, port, rail system or any other public facility of a similar nature as may be notified by the Board in this behalf ;

(*ii*) a water supply project, irrigation project, sanitation and sewerage system ;

(*iii*) a project for generation, or generation and distribution of electricity or any other form of power ;

(*iv*) a project for providing telecommunication services.

58. Income of Registered Trade Unions [Section 10(24)]

The following incomes of registered trade unions are exempt from tax:

(*i*) Income from house property.

(*ii*) Income from other sources.

The trade union must be a registered one and formed primarily for the purpose of regulating the relations between workmen and employer or between workmen and workmen. This benefit shall also be available to an association of registered trade unions.

59. Income of Provident and Superannuation Funds [Section 10(25)]

(*i*) Interest on securities which are held by or are the property of any provident fund to which Provident Funds Act, 1925 applies and any capital gains of the fund arising from the sale, exchange or transfer of such securities.

(*ii*) Any income received by the trustees on behalf of a recognised provident fund.

(*iii*) Any income received by the trustees on behalf of an approved superannuation fund.

60. Income of Employee's State Insurance Fund [Section 10 (25A)]

Income of such fund is fully exempted from 1.4.1962.

61. Income of Schedule Tribe Members [Section 10(26)]

Certain type of incomes of the members of Scheduled Tribes living in tribal areas are exempt from tax. The Scheduled Tribes to which this exemption applies are

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defined in Clause (25) of Article 366 of the Constitution, residing in any areas specified in Part A or Part B of the table appended to paragraph 20 of the Sixth Schedule of the Constitution or in the State of Arunachal Pradesh, Manipur, Tripura, Mizoram and Nagaland.

The exempted incomes are incomes which accrue or arise to him:

(*i*) from any source in the area, State, or Union Territories aforesaid, or

(*ii*) by way of dividend.

62. Income of Persons of Ladakh [Section 10(26A)]

Any income accruing or arising to any person from any source in the district of Ladakh or outside India in any previous year relevant to any assessment year commencing before the 1st day of April, 1989 where such person is resident in that said district in that previous year.

Provided that this clause shall not apply in the case of any such person unless he was resident in that district in the previous year relevant to the assessment year commencing on 1.4.1962.

63. Income from Lottery in State of Sikkim [Section 10(26AA)]

In case any person wins a prize from any Lottery the draw of which is held as a result of an agreement signed before 1.4.89 between State of Sikkim and any Lottery agent, such prize shall be exempted provided such person is resident of the State of Sikkim during relevant previous year.

For becoming the resident of the State of Sikkim, the person shall have to fulfil the conditions given u/s 6(1), 6(2), 6(3) and 6(4) of the Act. In these sections wheresoever words *"in India"* are used, they will be deemed to have been replaced by the words "State of Sikkim" and in case of company, the resident company shall be that which is registered in the State of Sikkim.

This clause is being omitted with effect from assessment year 1998-99.

64. Income of a corporation set-up for promoting the interests of Scheduled Castes, Scheduled Tribes or Backward Classes [Section 10(26B)]

Income of such corporation or body, institutions or associations which are wholly financed by govt. and which have been set-up to promote the interest of above mentioned communities shall be fully exempted.

65. Income of a corporation set-up to protect the interests of Minorities [Section 10(26BB)]

Income of such a corporation is fully exempted.

66. Income of cooperative society looking after the interests of Scheduled Castes or Scheduled Tribes or Both [Section 10(27)]

Such income shall be fully exempted provided the membership of such society consists of only other cooperative societies formed for similar purposes and the finances of the society are provided by Government and such other societies.

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67. Income paid or adjusted under Tax Credit Certificates [Section 10(28)]

Any amount of income adjusted or paid in respect of tax credit certificates. This amount must be adjusted or paid according to the provisions of the Act regarding tax credit certificates.

This clause is being omitted with effect from assessment year 1998-99.

68. Income from letting of godowns, warehouses etc. to a specified authority [Section 10(29)]

The income of an authority set up for purpose of marketing of commodities is exempted from income-tax. The exempted income in this case should be derived from the letting of godowns or warehouses for storage, processing or facilitating the marketing of commodities.

69. Amount received as subsidy from or through the Tea Board [Section 10(30)]

This exemption is available to assessee carrying on the business of growing and manufacturing tea in India. The subsidy received by such assessee from or through the Tea Board under any such scheme for replantation or replacement of tea bushes or for rejuvenation or consolidation of areas used for tea cultivation *(inserted by Finance Act, 1984)* as the Central Government may notify in the Official Gazette is exempt. For getting this exemption, the assessee is required to furnish to Assessing Officer, along with his return of income a certificate from the Tea Board showing the amount of subsidy received by him during the previous year. The A.O. may allow the assessee such time as he thinks desirable and the assessee is required to submit the said certificate within the allowed time.

70. Amount received as subsidy from or through the concerned Board [Section 10(31)]

Any amount received as subsidy from or through the concerned Board for replantation or replacement of Rubber, Coffee, cardamom plants or plants for growing of such other commodities or for any other scheme so notified shall be fully exempted.

71. Income of child clubbed u/s 64 (1A) [Section 10(32)]

In case income of a minor child is clubbed with the income of his parent, the parent can claim exemption upto actual income of child clubbed or Rs. 1,500 whichever is less in respect of each minor child whose income is included.

72. Income from dividends [Section 10(33)]

With effect from assessment year 1998-99 any amount declared, distributed or paid by Indian domestic company, by way of dividends whether interim or otherwise on or after 1.6.1997 whether out of current or accumulated profits shall be fully exempted.

TAX FREE ZONES u/s 10A

With effect from 1.4.1981, if any industrial undertaking is set up by any assessee in free trade zones and fulfil the other conditions as laid down for this

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purpose, the income of such assessee from such industrial undertakings shall be exempt from tax. The exemption has been introduced to encourage establishment of export-oriented industries in the 'Free Trade Zones'. This tax-holiday benefit shall be available for a period of 5 years in lieu of other concessions.

Rate of Exemption [Section 10A(1)]. Any profits and gains derived by an assessee from an industrial undertaking to which this section applies shall be fully exempted from tax and shall not be included in the total income of the assessee.

Eligibility [Section 10A(2)]. This exemption shall be available to any industrial undertaking which fulfils the following conditions, namely:

(*i*) (*a*) It has begun or begins to manufacture or produce articles or things during the previous year relevant to the assessment year commencing on or after 1st April 1981 in any 'free trade zone'.

(*b*) It begins to manufacture or produce the articles or things during the previous year relevent to the assessment year commencing on or after 1.4.94 in any electronic hardware technology park or, as the case may be, in software technology park.

These parks are to be set up under the Electronic Hardware Technology Park (EHTP) Scheme or under Software Technology Park Scheme notified by Government of India, Ministry of Commerce.

The articles or things to be produced shall include production of computer programmes.

The word 'Manufacture' shall include:

(*a*) process; or

(*b*) assembling; or

(*c*) recording of programmers on any disc, tape, perforated media or other information storage device.

This has been made effective from 1.4.1981.

(*ia*) Any undertaking which begins to manufacture article or a thing after 1.4.1995, its exports must be not less than 75% of its total sales during the previous year.

(*ii*) It is not formed by the splitting up or the reconstruction of a business already in existence. (This provision shall not be applicable to the undertaking claiming benefit under section 33B, *i.e.*, Rehabilitation allowance); and

(*iii*) It is not formed by the transfer to new business of machinery or plant previously used for any other purpose.

Period of Exemption [Section 10A(3)]. The profits and gains of eligible industrial undertakings shall not be included in the total income of the assessee for a period of 5 consecutive previous years out of a period of 8 previous years beginning with the assessment year relevant to the previous year in which undertaking has commenced its operations.

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'Free Trade Zone'—Defined

Free trade zone includes any zone which the Central Government may by notification in Official Gazette specify for the purposes of this section.

These notified zones are:

1. Kandla Free Trade Zone
2. Santacruz Electronics Export Processing Zone
3. Falta Export Processing Zone
4. Madras Export Processing Zone
5. Cochin Export Processing Zone
6. NOIDA Export Processing Zone.

Withdrawal of certain benefits [Section 10A(4)]

1. For calculating the profits of this business, the effect shall have to be given to the provisions relating to depreciation, investment allowance, development allowance, rehabilitation allowance, and different deductions admissible under sections 35 and 36(1)(ix). But the facility of carry forward of unabsorbed depreciation [32(2)], Investment allowance [32 A(3)(iii)], Expenditure on Scientific Research [35(4)] and Expenditure on Family Planning [36(1)(xi)] shall not be available to the assessee claiming this exemption during the previous year relevant to the assessment years immediately succeeding the last of the relevant assessment years or any previous year relevant to any subsequent assessment year.

2. During the period mentioned above, the benefit of carry forward of business loss [72(1)], loss on capital assets [74(1)] and unabsorbed portion of tax holiday benefits u/s 80J also shall not be available to the assessee.

3. Industrial undertaking shall not be entitled to claim deduction under section 80HH, 80HHA or 80I where it begins or has begun to manufacture or produce, articles or things during any previous year relevant to any of the relevant assessment years.

4. While computing written down value of the assets for the purpose of computation of depreciation under section 32 full amount of depreciation shall be deducted in respect of each of the relevant assessment years.

Relaxation of Eligibility [Section 10A(5)]

This benefit shall be available to those industrial undertakings which have begun to manufacture or produce articles or things in any previous year relevant to assessment year commencing on or after the 1st day of April 1977 but before 1st day of April 1981. In such case, assessee, if he so desires, may furnish to the Assessing Officer a declaration in writing that the provisions of this exemption may be applied to him for each of the relevant assessment years as reduced by the number of assessment years which have expired before 1st April 1981. He must submit this declaration before the expiry of date of filling of return, whether originally fixed or extended, for the assessment year commencing on 1st April 1981.

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Option to Assessee [Section 10A(7)]

The person who is entitled to claim this benefit can exercise the option of not availing this benefit by furnishing in writing a declaration to the Assessing Officer before due date of filing of return.

TAX EXEMPTION FOR 100% EXPORT-ORIENTED UNDERTAKING [SECTION 10B]

The Finance Act, 1988 has introduced this provision with effect from 1.4.89, *i.e.*, assessment year 1989-90.

1. Rate of Exemption [Section 10B(1)]

Any profits and gains derived by an assessee from a hundred per cent export-oriented undertaking to which this section applies shall not be included in the total income of the assessee.

2. Eligible Undertaking [Section 10B(2)]

Any undertaking must fulfil the following conditions to qualify for this benefit:

(*i*) It manufactures or produces any article or thing.

(*ia*) In relation to an undertaking which begins to manufacture or produce any article or thing on or after 1-4-1994, its exports of such articles or things are not less than 75% of the total sales thereof during the previous year.

(*ii*) It is not formed by the splitting up or the reconstruction of a business already in existence.

(*iii*) It is not formed by the transfer to a new business of machinery or plant previously used for any purpose unless it is imported from outside India.

3. Period of Exemption [Section 10B(3)]

Assessee has been given the option to choose a period of consecutive 5 years falling within a period of 8 years beginning with the assessment year relevant to the previous year in which undertaking commenced its operations.

4. Withdrawal of certain benefits [Section 10B(4)]

(*i*) Facility of carry forward of unabsorbed depreciation, investment allowance, capital expenditure on family planning shall not be admissible.

(*ii*) Any loss relating to relevant assessment years cannot be C/F.

(*iii*) No deduction u/s 80HH, 80HHA or 80I.

(*iv*) Full depreciation will have to be deducted to calculate W.D.V. of assets.

5. Units commencing production before 1.4.89 [Section 10B(5)]

Such units can also opt for this benefit if they give a declaration, before due date of filling of return, regarding its intention to avail this benefit.

6. Option to Assessee [Section 10B(6)]

The person who is entitled to claim this benefit can exercise the option of not availing this benefit by furnishing in writing a declaration to the Assessing Officer before due date of filing of return.

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7. Hundred per cent export-oriented undertaking [Explanation to Section 10B]

Any undertaking which has been approved as a 100% export-oriented undertakings by the Board appointed in this behalf by the Central Govt. in exercise of the powers conferred by section 14 of the Industries (Development and Regulation) Act 1951 and rules made under that Act.

POWERS OF CENTRAL GOVERNMENT

With effect from 1.4.81, Government of India has empowered itself to declare income to a particular person as exempted from tax by insertion of new section 293A in the Income-tax Act.

The general provisions of this section are:

1. If the Central Government is satisfied that it is necessary or expedient so to do in the public interest, it may, by notification in the Official Gazette, make the income of certain persons or class of persons, fully or partially exempt from tax or reduce or make certain modifications in respect of income-tax in favour of such persons.

2. **Persons Defined.** The persons referred above are namely:

(*i*) The persons with whom the Central Government has entered into agreements for the association or participation of that Government or any person authorised by that Government in any business consisting of the prospecting for or extraction or production of mineral oils;

(*ii*) The person rendering technical services in connection with any business consisting of the prospecting for or extraction or production of mineral oils carried on by that Government or any person specified by that Government in this behalf by notification in the Official Gazette; and

(*iii*) Employees of the person referred to in points (*i*) and (*ii*) above.

The insertion of this section has become essential due to extension of Income-tax Act, 1961 to offshore areas but to keep the oil extraction business free from the tax provisions, the Government has taken over these powers to declare the income of such persons or their employees who are engaged in the business of prospecting or extraction or production of mineral oils as exempted.

Illustration. In the following cases, state whether the receipts are taxable or not. Give reasons for your answers :

(*a*) Salary income received by X, as general manager of M/s A & Co. who derives its full income from agricultural crop produced on its own land.

(*b*) Y, a film actress, is awarded a cash prize of Rs. 1,00,000 under the scheme of State awards for actresses. Y claims this to be exempt from tax as a casual receipt.

(*c*) X, Y and Z are the three medical practitioners who have formed a partnership to establish and run a nursing home. For the accounting year ended on 31st March, 1997 the profits of the nursing home amounted to Rs. 1,20,000 which are claimed by the partners as exempt under Section 10(22A) of the income tax Act, 1961.

[*Company Secretary (Inter) June, 1991*]

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Solution

(*a*) Remuneration received by Mr. X is for services rendered to M/s A & Co. and so it is to be treated as salary income and will be fully taxable. Source of income of Mr. X is services rendered to the company and not from agricultural activity. Nature of the income in the hands of the payee is not relevant for the receiver of this income. Income of the company shall, of course, be agricultural income and exempt from tax.

[*Premier Construction Co. v. C.I.T.*]

(*b*) Cash prize received by a film actress cannot be treated as casual income and exempted only upto Rs. 5,000 but it should be treated as fully exempted u/s 10(17A)(i) provided the award satisfies the conditions laid down in that sub-section. The important conditions are that the prize should be in public interest and approved by the Central government in that behalf.

(*c*) The profit of Rs. 120,000 earned by a nursing home cannot be treated as exempted u/s 10(22A) because the exemption under this section is allowed only if hospital is set-up solely for philanthropic purposes and not for earning of profit. In this case the partnership firm is set-up for earning of profit and so the claim of partners regarding the exemption of profit is untenable.

QUESTIONS

1. Discuss the incomes which are not included in total income nor income-tax is payable on them. [*B.Com. Hons., Delhi*]
2. Give ten examples of incomes which are totally exempt from income-tax.
3. Write short note on Casual Income.
4. Explain the provisions of law relating to tax holiday in respect of Free Trade Zones. [*B.Com. Punjab, Sept., 1986*]
5. Write one paragraph of about 100 words on following terms:
   - (*i*) Casual Income
   - (*ii*) House Rent Allowance
   - (*iii*) Gratuity
   - (*iv*) Technicians working in India under Technical Assistance Programme
   - (*v*) Leave Travel Concession
   - (*vi*) Interest paid to non-residents
   - (*vii*) Commuted Pension
   - (*viii*) Interest exempted u/s 10(15)
   - (*ix*) Tax Exemption for 100% export-oriented units.

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PART II

COMPUTATION OF TOTAL INCOME
(FOR ASSESSMENT YEAR 1997-98)

1 SALARIES

2 INCOME FROM HOUSE PROPERTY

3 PROFITS AND GAINS OF BUSINESS OR PROFESSION—I

4 PROFITS AND GAINS—II—DEPRECIATION

5 CAPITAL GAINS

6 INCOME FROM OTHER SOURCES

7 AGGREGATION OF INCOME

8 CARRYING FORWARD AND SET OFF OF LOSSES

9 DEDUCTIONS TO BE MADE OUT OF GROSS TOTAL INCOME

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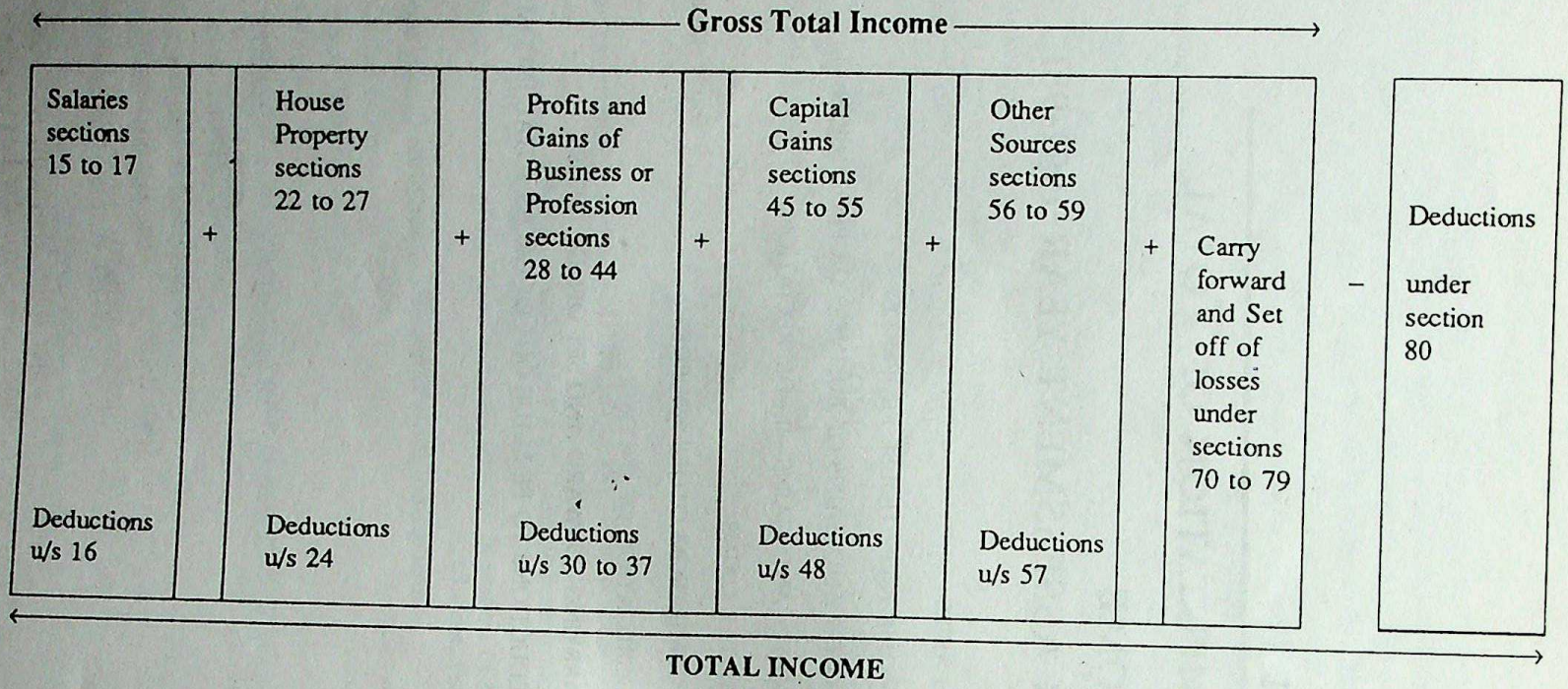
CONCEPT OF TOTAL INCOME



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1 SALARIES

Computation of Total Income—Definition of head salary—Characteristics of salary—Computation of salary income—salary u/s 17(1)—annual accretion—Allowances—Perquisites and their types and treatment—Profits in lieu of salary and exempted profits—Deductions u/s 16—Illustrations—Rebate of Tax u/s 88—Chart—Illustrations and Questions.

COMPUTATION OF TOTAL INCOME

According to section 4 of the Income-tax Act 1961 tax is to be charged on total income of an assessee relating to previous year in the assessment year. Total income is defined u/s 2(45) as the total income defined in section 5 and to be computed in the manner as laid down in section 14 of the Act. Section 5 provides the basis for the computation of total income and which is based upon residential status of the assessee in relevant previous year.

Section 14 of Income-tax Act 1961 provides for the computation of total income of an assessee which is divided under five heads of income. Each head of income has its own method of computation. These five heads are:

(*i*) Income from 'Salaries';
(*ii*) Income from 'House Property';
(*iii*) Income from 'Profits and Gains of Business or Profession';
(*iv*) Income from 'Capital Gains'; and
(*v*) Income from 'Other Sources'.

Income from all these heads shall be computed separately according to the provisions given in the Act. Income computed under these heads shall be aggregated after adjusting past and present losses and the total so arrived at is known as 'Gross Total Income'.

Out of Gross Total Income, Income-tax Act 1961 allows certain deductions under section 80. After allowing these deductions the figure which we arrive at is called 'Total Income' and on this figure tax liability is computed at the prescribed rates.

These five heads of income are water tight compartments. Income from one source of Income, which is to be included in a particular head, cannot be included in any other head. Each head of income has its own deductions. After computing income from various sources of income within a particular head its own deductions are allowed and thus we arrive at income from that head. (See Chart on page 2/2).

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In the next few chapters the method of computation of income under each head is given. After that the next chapter deals with the adjustment of losses. Last chapter of this part deals with deductions to be given from gross total income.

HEAD SALARIES DEFINED

Under section 15, the following incomes are chargeable to Income-tax under the head 'Salaries';

(*a*) any *salary due* from an employer or a former employer to an assessee in the previous year *whether paid or not;*

(*b*) any *salary paid or allowed* to him in the previous year by or on behalf of an employer or a former employer *though not due* or before it becomes due to him;

(*c*) any *arrears of salary* paid or allowed to him in the previous year by or on behalf of an employer or a former employer if not charged to income-tax for any earlier previous year.

Under the provisions of this section the amount of salary due in the year, amount of advance salary received and the amount of arrears of salary received during the year from the present or past employer are to be included in this head.

In the explanation attached to section 15, it has been clearly mentioned that for the removal of doubts, it is hereby declared that where any salary paid in advance is included in the total income of any person for any previous year it shall not be included again in the total income of the person when the salary becomes due.

The important rule is that income once taxed cannot be taxed again, so any salary paid in advance (if taxed in a previous year when the advance salary was received) will not be included again in the total income of the person when the salary becomes due. Advance salary does not include loans, *e.g.*, loan to purchase a car or a scooter or for building a house etc.

Any salary, bonus, commission or remuneration, by whatever name called due to or received by a partner of a firm from firm shall not be regarded as salary for the purposes of this section.

CHARACTERISTICS OF SALARY

For any payment to be made taxable under the head 'Salaries' it must fulfil the following characteristics. In case any receipt is not covered under any of these features it will not come under this head:

1. Relationship of employer and employee

For a payment to fall under the head 'Salaries' the relationship of employer and employee must exist between payee and the receiver of the salary. The employer may be a Government, a Local authority, a company or any other public body or an Association or H.U.F. or even an individual. Every kind of payment to every kind of servant, public or private, however high or low placed he may be, is covered under the provisions of this Act. Even the remuneration payable to an employee of a foreign Govt. falls within this section. Even servant is an employee, but an agent may or may not be employee. A detailing agent of a selling concern is its employee whereas the person holding an agency to sell the goods of such a concern will not be employee. The relationship of master and servant is the only test to establish the relationship of employer and employee. A director of a company, though holding an

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office, is not an employee unless it is so provided in the independent contract, or the Articles of Association of the company provide for such a relationship.

[Ram Prashad v. C.I.T. (86 I.T.R. 122, 127 (S.C.)]

Sometimes, the employer allows an employee to draw tax-free salary, *e.g.*, the employer pays full salary to the employee and also pays tax on this directly to the department. The employee's assessment is to be made not on the amount of salary he is drawing but on gross amount *i.e.*, salary drawn plus the tax paid by the employer.

2. Salary received as Member of Parliament

Salary received by a member of Parliament is not taxable under the head 'Salaries'. It is taxable as income from other sources'. Any allowance received by them is fully exempted from tax.

3. Receipts from Persons other than Employer

Perquisites or benefits or any other remuneration received from persons *other than the employer*, would be taxable not under the head 'Salaries' but under the head 'income from other sources' even if they accrue to the employee by reason of his employment or while he was discharging his normal duties, *e.g.*, amount received by a professor of a college for acting as an examiner in a university.

For example, Dr. Dhir is an employee of a leading physician of Delhi. In one case, the patient's life was saved because of the hard work and intelligence of Dr. Dhir. The patient, therefore, gives Rs. 5,000 to Dr. Dhir in appreciation of his services. The amount in this case is not chargeable as 'salary' but constitutes income from other sources.

4. Place of Accrual of Salary Income

Salary accrues at that place where the services are rendered. If the services are rendered in India, the salary accrues in India and if the services are rendered outside India, the salary accrues outside India. Thus, if a person employed in India goes on leave to England and gets his leave salary there, the salary is said to accrue in India and not in England, because it is paid for services rendered in India. Pension paid in a foreign country for services rendered in India, will be Indian income, as it is paid for the services rendered in India although in the past. On the other hand, if any person is employed in India and transferred to its branch in England, the salary received by him in England is not Indian income, but it is income arising in England as the service is rendered in England. Followings are the *two exceptions* to this rule:

(*i*) *A pension payable outside India* to a person who has gone to foreign country for permanent settlement is not deemed to arise in India, if pension is payable to a person appointed by the Secretary of State or to a person who was appointed before 15th August 1947, as a judge of the Federal Court or of a High Court and who continued to serve on or after the commencement of the Constitution as a judge in India. This is a special concession granted to certain officials of Government, who were employees before independence but continued to serve after this.

(*ii*) *The Govt. of India employs Indian citizens for services to be rendered in foreign countries* and salary paid outside India is deemed to accrue or arise in India.

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This provision helps in taxing the salaries received by Government servants posted abroad. But under Section 10(7) the allowances and perquisites paid or allowed by the Government outside India are to be excluded from total income.

5. Deductions made by the Employer

If, an employer makes certain deductions out of the salary payable to an employee, amount so deducted is deemed to be received by the employee and the amount so deducted is also taken as application of income by the employee. Some important types of deductions made by the employer are as follows:

1. Deductions made to recover the loan advanced by the employer.
2. Employee's contribution towards the provident fund, income-tax and profession tax.
3. Deduction made to pay the premium on life insurance policy of the employee.
4. Any other deduction for which the employee has authorised the employer.

In case an employee receives his salary after certain deductions made by employer on account of profession tax, contribution to provident fund, tax deducted at source, the 'salary' will not be the net amount received, rather it will be the gross salary due to the employee.

Example. Mr. A receives Rs. 63,500 p.a. as net salary. Employer had deducted Rs. 7,500 as Employee's contribution to R.P.F. Rs., 1,300 p.a. as tax deducted at source and Rs. 1,200 p.a. as professional tax. During the year employer had deducted Rs. 2,500 towards the recovery of house building advance taken by Mr. A.

In the above-mentioned case employee's salary is not Rs. 63,500 rather it will be:

			Rs.
		Net salary received	63,500
Add:	(*i*)	Employee's own contribution to P.F.	7,500
	(*ii*)	Tax deducted at source	1,300
	(*iii*)	Professional tax deducted at source	1,200
	(*iv*)	Recovery of House Building Advance	2,500
		Salary	76,000

But sometimes salary is given at a particular rate and tax deducted at source, own contribution to P.F. and recovery of loan etc. are given. In such a case these deductions are not to be added back as the salary given is not after deduction of these amounts rather it is given before deduction of these items.

6. Salary or Pension received by UNO Employees

It is fully exempted as per circular No. 293 Dt. 10.2.81.

7. Salary as Partner

Any salary, commission or remuneration received by a working partner from a firm assessed as firm shall not be taxable under the head 'Salaries'. It is taxable under the head Profits & Gains.

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8. Payments received by legal heirs of a deceased Employee

Any ex-gratia payment or compensation given to widow or legal heirs of an employee who dies during service is not taxable as salary income but family pension received is taxable under 'other sources'.

9. Payment made after Cessation of Employment

Payment made by an employer to his employee after the cessation of his employment is also taxable under the head 'Salaries'. It is taxable under this head because it represents remuneration for services rendered in the past.

10. Voluntary foregoing: Application of Salary

Voluntary foregoing of salary by an employee is simply an application of income by him and, therefore, any voluntary foregoing of salary is taxable when it is due, whether paid or not (Section 15). The salary which is voluntarily foregone must be actually due in the name of the employee. Voluntary foregoing is different from voluntary surrender of salaries which is exempted from tax.

11. Previous year for Salaries

The previous year for the income under the head 'Salaries' shall always be financial year of the Government of India (*i.e.*, April to March).

12. Salary when due?

Salary becomes due on the first date of every month. In almost all the offices of State Government this rule is in force. In Central Government offices the salary is paid on the last date of the month but salary for the month of March is paid only on 1st April. In these cases, in a particular assessment year, the salary drawn by the employee for the month of March paid in April to February paid in March shall be included.

In banks and certain other bodies, the salary is credited on the last date of the month. Hence, the salary from April to March next shall be taxable.

Illustration 1. Mr. A is a Government employee and is getting Rs. 1,500 p.m. as salary. He gets his increment of Rs. 100 on 1st Jan. every year. What will be his salary for the previous year 1996-97 ?

Solution

As Mr. A is a Government employee and his salary becomes due on the first day of every month, the amount received by him from the month of March paid in April 1996 to February paid in March, 1997 shall be included. As such his salary received upto 1st Jan. 1997, *i.e.*, for 10 months shall be @ Rs. 1,500 p.m. and for 2 months it shall be @ Rs. 1,600 p.m.

Had he been a bank employee, the amount received would have been @ Rs. 1,500 for 9 months and @ Rs. 1,600 for three months.

Q. No. 1

Mr. Sen was appointed as Reader in Calcutta University in the scale of 3700—125—4950—150—5700 on 1.9.92. Compute his salary income for the previous year 1996-97 if (a) salary is due on 1st of every months; (b) salary is due on last date of every month.

[Hints (a) Salary Rs. 49,650 (b) Rs. 49,775]

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13. Advance salary received

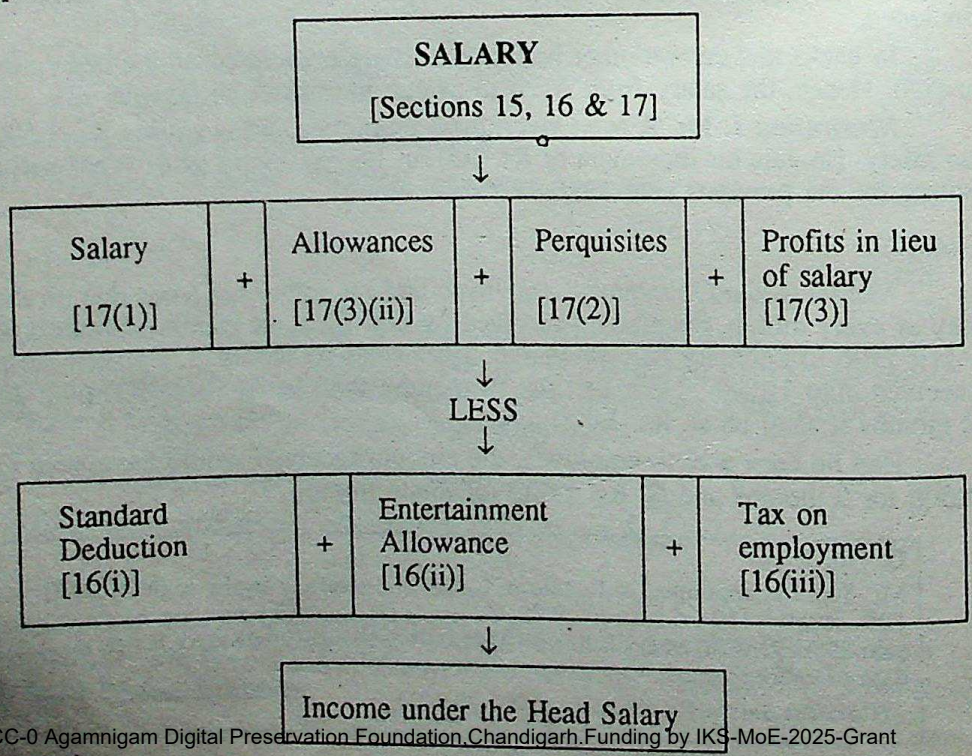
In case an assessee receives some salary in advance in a previous year which was actually not due in that year, it shall be taxable in the year of receipt. In case, any loan or advance is taken it is not treated as advance salary.

14. Arrears of salary received

Any amount of salary received from present or past employer during relevant previous year and which relates to some earlier previous years, is treated as arrears of salary. It is taxable in the year in which received and not the year to which it belongs. *[C.I.T. v. Gajapathy Naidu (1964) 58 I.T.R., 114 (S.C.)]*. In case assessee has to pay tax at a rate higher than that at which he would have paid, had these arrears been received in the year to which they belong, assessee can apply to Income-tax Officer for relief u/s 89(1) (Refer to Chapter 2 of part III of this book).

COMPUTATION OF SALARY INCOME

Salary income of an employee is to be computed in accordance with the provisions laid down in sections 15, 16 and 17. Section 15, as discussed earlier gives the scope of this head and tells us that which incomes shall form part of this head. Section 16 gives deductions to be allowed out of incomes taxable under this head. Section 17(1) defines the word 'salary' as mentioned in section 15. Section 17(2) and 17(3) further define the terms 'Perquisites' and "profits in lieu of salary". These can be depicted in the form of chart given below:



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Definition of word 'Salary' [Section 17(1)]

According to Section 17(1) salary includes the following amounts received by an employee from his employer, during the previous year:

(*i*) *Wages;*

(*ii*) *any annuity or pension; (Family pension received by heirs of an employee is taxable under income from other sources);*

(*iii*) *any gratuity;*

(*iv*) *any fees, commission, perquisites or profits in lieu of or in addition to any salary or wages;*

(*v*) *any advance of salary;*

(*va*) *any payment received by an employee in respect of any period of leave not availed of by him; (Leave encashment or salary in lieu of leave);*

(*vi*) *the annual accretion to the balance at the credit of an employee participating in a recognised provident fund, to the extent to which it is chargeable to tax under Rule 6 of part A of the Fourth Schedule; and*

(*vii*) *the aggregate of all sums that are comprised in the transferred balance as referred to in sub-rule (2) of Rule 11 of Part A of the Fourth Schedule, of an employee participating in a recognised provident fund, to the extent to which it is chargeable to tax, under sub-rule (4) there, i.e., taxable portion of transferred balance from unrecognised provident fund to recognised provident fund.*

The above definition of word *'salary'* u/s 17(1) includes the above mentioned items. These can be explained in following manner:

(*i*) *wages*—any amount received by a person for work done or job rendered is called wages. It may be received under the name of 'Pay', 'Basic Pay', 'Salary', 'Basic salary' or 'Remuneration'. It may be for actual work or leave salary or actually received or due during the relevant previous year. *Salary in lieu of Notice*. It is fully taxable u/s 15 if received during the relevent previous year.

(*ii*) *any annuity or pension*—Any amount received by employee from past employer after attaining the age of retirement or superannuation is fully taxable. It may be received direct as pension or out of a superannuation fund created by employer; in both cases it is taxable.

(*iii*) *any gratuity*—Any sum received by employee from his past employer as a token of gratitude for services rendered in past is called gratuity. This amount is exempted upto certain limits given u/s 10(10) and it is dealt with in this very chapter at a later stage.

(*iv*) (*a*) *any fee*—any amount received from employer under the name of fee is also fully taxable.

(*b*) *any commission*—any commissions given by employer to employee is fully taxable. Any commission received by a director for standing guarantee for repayment of loan, and if he is not employee of the company, shall be taxable under "Income from other sources". **In case commission is given to an employee and it is based upon *turnover achieved by such employee*, such commission shall also be treated**

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as part of the salary for all practical purposes. [*Gestener Duplicators (P) Ltd. vs. C.I.T. (1979) SC*].

(*c*) *any Bonus*—Bonus is fully taxable under the head 'Salaries' on receipt basis. In case arrears of bonus are received in a previous year, these are fully taxable. Bonus can be of two types:

(A) *Statutory Bonus*—It is received under some legal or contractual obligation and is fully taxable.

(B) *Gratuitous Bonus*—It is a casual benefit and is taxable as a receipt from employer and having no other implication.

(*d*) *any Perquisite*—Any benefit or amenity allowed by employer to employee. These are explained in detail later in this chapter u/s 17(2).

(*e*) *any Profit in lieu of or in addition to salary*—any cash payment received by employee from employer is called profit in lieu of salary and these are explained later in this chapter u/s 17(3).

(*v*) any salary in lieu of leave received during service is fully taxable.

(*vi*) *any advance salary*—In case an assessee receives some salary in advance in a previous year and which was actually not due in that year shall be taxable in the year of receipt. It does not include any loan or advance taken from employer.

(*vii*) *Annual accretion to R.P.F.* and

(*viii*) *Taxable portion of transferred Balance of U.R.P.F.*

Detailed treatment of these two points is given after discussing the various types of provident funds.

PROVIDENT FUNDS

To encourage savings for the social security of employees, the Government has set up various kinds of provident funds. The employee contributes a fixed percentage of his salary towards these funds and in many cases employer also contributes. The whole contribution along with interest is credited to employee's account. He will get payment out of this fund at the time of retirement and at some other important occasions. If the employee dies, his heirs will get the full payment.

Provident Funds are of four kinds:

(*i*) Statutory Provident Fund or the Fund to which the Act of 1925 applies (S.P.F.).

(*ii*) Recognised Provident Fund (R.P.F.).

(*iii*) Unrecognised Provident Fund (U.R.P.F.).

(*iv*) Public Provident Fund (P.P.F.).

(i) Statutory Provident Fund. Statutory provident fund is the oldest type of fund. It was started in the year 1925 through a Provident Fund Act of 1925. This fund was started with a view of promoting savings amongst government employees. Generally, this fund is maintained by Government or Semi-Government Departments like Railways, Reserve Bank of India, Colleges, Universities, local bodies, insurance companies, etc.

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(Continued on Page 12)

TREATMENT OF PROVIDENT FUNDS

Particulars	*Fund governed by P.F.* Act 1925 (S.P.F.) (For Govt. or Semi Govt. Employees)	*Recognised Provident Fund* (R.P.F.) (For Private Sector)	*Unrecognised P.F.* (U.R.P.F.) (For Private Sector)
1. Employee's own contribution.	Fully qualifies for rebate u/s 88	Fully qualifies for rebate u/s 88	Does not qualify for rebate u/s 88.
2. Employer's contribution	Fully exempted	It is deemed to be received by employee. Excess of Employer's contribution to R.P.F. over 10% of salary is taxable.	Ignore for the time being.
3. Interest credited to Accumulated Balance.	Fully exempted	Exempted upto rate prescribed by the Government. Excess over this amount is taxable (i.e. 12%) above 12%	Ignore for the time being.
4. Refund/Transferred Balance of U.R.P.F. to R.P.F.	Fully exempted	Exempted in all cases except when employee leaves service of his own accord before completion of 5 years' continuous service. In such case the amount which has not been charged to tax is added in salary	In case of refund taxable portion[1] is added in salary income of the year [Entitled to relief u/s 89(1)]. In case transferred balance amount which would have been taxable had the fund been RPF is added in salary

1. Taxable Portion = Employer's contribution + Interest on this part. Interest on employee's own contribution is taxable under the head Income from Other Sources.

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The employer's contribution towards the employee's statutory provident fund and the amount of interest earned on the accumulated balance to the employee's credit balance are not to be included in the income of employee and so it is ignored.

When the employee retires or leaves the service and receives any amount from the accumulated balance to his credit in the statutory provident fund, the amount so received will not be included in employee's total income [Section 10(11)] being exempted income.

The employee's own contribution will qualify for rebate u/s 88.

(ii) Recognised Provident Fund. As the name suggests, it is a fund to which the Commissioner of Income-tax has given the recognition as required under the Income-tax Act. Generally this fund is maintained by industrial undertakings, business houses, banks, etc.

The employer's contribution over and above 10% of employee's salary, will be included in employee's salary income for tax purposes.

The employee's contribution towards this fund will fully *Qualify* for rebate u/s 88.

Interest on Provident Fund credit balance upto prescribed rate (12%) is exempted, but interest credited over and above such rate is deemed to be employee's salary income and is included in salary income of that previous year.

(iii) Unrecognised Provident Fund. It is the provident fund which is not recognised by the Commissioner of Income-tax. The employee and the employer both contribute towards this fund.

The employee's contribution is added in this salary (if 'net salary' or 'salary after deduction of' is given) and he will not be allowed any rebate of tax regarding this contribution while computing the total tax of the employee.

The employer's contribution and interest on the accumulated credit balance of the fund are not to be included in employee's salary income from year to year.

A payment received out of this fund is taxable so far it represents the employer's contribution and interest thereon. The employee is entitled to relief under section 89(1). [The employee's contribution is ignored because it was taxed when it was contributed]. Interest on the employee's own contribution will be taxable as 'Income from Other Sources' and not as salary income.

Transferred balance. When the unrecognised provident fund is recognised for the first time, the credit balance in the employee's unrecognised provident fund is transferred to the recognised provident fund account. This balance is known as transferred balance. In such case fund will be treated as RPF from the day of its inception as exemption will be allowed in same manner. Only excess of amount transferred to RPF over exempted amount shall form taxable portion of transferred balance.

(iv) Public Provident Fund. So far all these funds were for the salaried people. On July 1, 1968 a new fund known as public provident fund was started so that self-employed people may also enjoy the benefit of rebate under Section 88. Self-employed people are doctors, lawyers, accountants, actors, traders, pensioners. This fund can suit all types of pockets and its working is also very simple. The interested people can open their account in State Bank of India and its subsidiaries. The

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subscription can be between Rs. 100 and Rs. 60,000 in one year. At one time one can deposit in multiples of 5 (For example, 10, 25, 45, 105, 225 etc.) and in one month only one deposit is possible and in the year minimum subscription should be Rs. 100 and the maximum Rs. 60,000.

Full withdrawal is possible after 15 years but in case of death of the subscriber full repayment will be made to the legal heir of nominee. Partial withdrawal and loans are also possible.

The subscription towards this type of fund is eligible for rebate in the similar manner, as in the case of statutory provident fund.

Balances in the public provident fund are not liable to attachment by any court.

Annual accretion [Section 17(1)(vi)]. The Rule 6 of Part A of Fourth Schedule defines taxable annual accretion as:

"That portion of the annual accretion in any previous year to the balance at the credit of an employee participating in a recognised provident fund as consists of—

(*a*) Contribution made by the employer in excess of ten per cent (10%) of the salary of the employee; and

(*b*) *Interest credited on the balance* to the credit of the employee in so far as it exceeds the amount allowed at a rate exceeding such rate as may be fixed by the Central Government in this behalf by notification in Official Gazette, shall be deemed to have been received by the employee in that previous year and shall be included in the total income for that previous year and shall be liable to income-tax.

The above-mentioned rule makes it clear that any contribution by employer to R.P.F. in excess of 10% of employee's salary is to be added in salary.

About interest the taxable portion will be excess of Interest credited to the balance of R.P.F. over a rate of interest to be announced by the Government from time to time.

Since the Government has increased the rate of interest in case of Statutory Provident Fund and Employee's Provident Fund to 12% p.a.—this exemption limit has also been raised to 12% by the Government.

To simplify the above discussion it can be put in the following manner—

Taxable annual accretion will consist of:

(*a*) Excess of employer's contribution to Recognised Provident Fund over 10% of employee's salary, and

(*b*) Excess of interest credited to R.P.F. over interest calculated at prescribed rate (*i.e.*, 12%) of the balance standing to the credit of employee [*Vide* Notification No. S.O. 120 (E) dated 27.3.86].

Illustration 2. Calculate the taxable amount of annual accretion to R.P.F. if following information is provided by assessee:

(*i*) Pay @ Rs. 2,500 p.m.

(*ii*) Commission received by him on the basis of turnover achieved by him: Rs. 6,000;

(*iii*) Employer's contribution to R.P.F. @ 12% of salary;

(*iv*) Interest credited during the year to R.P.F. Balance @ 15% is Rs. 6,000.

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Solution. *Calculation of taxable portion of annual accretion.*

	Rs.	Rs.
(*i*) Employer's contribution to R.P.F. @ 12% of salary (12% of 36,000)	4,320	
Less 10% of salary being exempted	3,600	
Taxable Portion		720
(*ii*) Interest credited to R.P.F. Balance @ 15%	6,000	
Less exempted upto @ 12% (6,000 × 12/15)	4,800	
Taxable portion		1,200
Taxable portion of annual accretion		1,920

Note : Salary for the above purposes is pay + commission on the basis of turnover achieved by him.

Q. No. 2

Compute taxable part of annual accretion from information given below:

(*i*) Salary @ Rs. 4,800 p.m.
(*ii*) Commission @ 1% of turnover of Rs. 2,40,000 achieved by him during the previous year
(*iii*) Employer's contribution to R.P.F. @ 600 p.m.
(*iv*) Interest credited to R.P.F. balance @ 14% p.a. is Rs. 8,400

[**Hints.** Rs. 1200 + 1200 = Rs. 2400]

Transferred Balance [Section 17(1)(vii)]

The balance of unrecognised provident fund, which is transferred to R.P.F. is called "*Transferred Balance*".

According to Schedule IV, rule 11(4), the amount of taxable portion will be calculated as under :

(*i*) The fund will be treated as R.P.F. from the date fund was instituted.
(*ii*) The employer's contribution of URPF shall quality for exemption upto 10% of salary and excess shall be taxable.
(*iii*) The interest credited to the accumulated balance shall be exempted if rate of interest was upto 12%. Excess if any is taxable.
(*iv*) The taxable amount under point (*ii*) and (*iii*) above shall be deemed to be the income of the previous year in which fund gets recognition. The remainder of the transferred balance shall be ignored.

Illustration 3. On 1.4.94 an employee starts contributing Rs. 300 pm to URPF and equal amount is credited by the employer. This practice continued till 30.9.96. Interest credited @14% for 1994-95 was Rs. 700, 1995-96 Rs. 1,400 and upto 30.9.96 Rs. 1,050. From 1.10.96 this fund is recognised by the Commissioner of Income-tax. Calculate the taxable amount of transferred balance if salary is due on last date of month and salary was Rs.2,500 pm (fixed) during this period.

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Solution. *Computation of taxable portion of transferred balance of U.R.P.F.*

	Rs.	Rs.
Previous year (1.4.94 to 31.3.95)		
Employer's contribution to URPF (Deemed RPF)	3,600	
Less Exempted @10% of salary	3,000	
Taxable Amount		600
Interest credited to URPF (Deemed RPF)	700	
Less exempted @12% (700 × 12/14)	600	
Taxable Amount		100
Previous Year (1.4.95 to 31.3.96)		
Employer's contribution to URPF (Deemed RPF)	3,600	
Less Exempted @10% of salary	3,000	
		600
Interest credited toURPF (Deemed RPF)	1,400	
Less Exempted @14% (1400 × 12/14)	1,200	
Taxable Amount		200
Previous Year (1.4.96 to 30.9.96)		
Employer's contribution to URPF (Deemed RPF)	1,800	
Less exempted @10% of salary	1,500	
Taxable Amount		300
Interest credited to URPF (Deemed RPF)	1,050	
Less exempted @12% (1,050 × 12/14)	900	
Taxable Amount		150
Taxable portion of Transferred Balance		1,950

Q. No. 3

Compute taxable portion of transferred balance of U.R.P.F. from information given below if it becomes R.P.F. from 1.10.96:

(*i*) Employee starts contributing Rs. 300 p.m. from 1.4.94 and continue to contribute to U.R.P.F. till 30.9.96.

(*ii*) Employer contributes an equal amount for the same period.

(*iii*) Interest credited @13% for the years 1994-95 Rs. 650, 95-96 Rs. 1,300 and from 1.4.96 to 30.9.96 Rs. 910.

(*iv*) He was drawing consolidated salary of Rs. 2,250 p.m. during this period and it was due on last date.

[**Hints.** Taxable portion of Transferred Balance Rs. 2,470]

ALLOWANCES [Section 17(3)]

A *Fully Exempted*	*B* *Fully Taxable*	*C* *Partially Taxable*
1. Foreign Allowance only in case of Govt. employees posted outside India	1 Dearness Allowance Additional D.A. High Cost of living allowance Interim Relief	1. House Rent Allowance 2. Allowances covered u/s 10 (14) (*i*) Helper Allowance (*ii*) Uniform Allowance (*iii*) Academic Allowance (*iv*) Conveyance Allowance

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A *Fully Exempted*	B *Fully Taxable*	C *Partially Taxable*
	2. City/Capital Compensatory Allowance	(*v*) Travelling Allowance
	3. Lunch Allowance	(*vi*) Any special allowance in the nature of Composite Hill compensatory Allowance or High Altitude Allowance or Uncongenial Climate Allowance or Snow Bound Area Allowance or Avlanche Allowance
	4. Tiffin Allowance	
	5. Marriage/Family Allowance	
	6. Deputation Allowance	
	7. Wardenship Allowance	
	8. Non practicing Allowance	
	9. Project Allowance	
	10. Overtime Allowance	
	11. Fixed Medical Allowance	(*vii*) Any Special Compensatory Allowance in the nature of border area or remote area or difficult area or disturbed area Allowance
	12. Entertainment Allowance	
		(*viii*) Tribal Area Allowance
		(*ix*) Running Allowance given to employees of transport sector,
		(*x*) Children Education Allowance
		(*xi*) Hostel Expenditure Allowance
		(*xii*) Compensatory Field Area Allowance
		(*xiii*) Compensatory Modified Field Area Allowance
		(*xiv*) Special Allowance in the nature of counter insurgency allowance given to the members of armed forces operating in areas away from their permanent locations for a period of more than 30 days.

A. Fully Exempted Allowance

Foreign Allowance—if given by Government to its employees posted abroad, under whatsoever name, it is fully exempted [Section 10(7)].

B. Fully Taxable Allowances

1. Dearness Allowance/Additional Dearness Allowance/High cost of living allowance/Interim Relief. These allowances are given by employer to the employees to meet the effect of rise in prices and these are fully taxable.

Some times it is mentioned that

(*i*) D.A. enters into pay for service benefits; or

(*ii*) D.A. enters into pay for retirement benefits; or

(*iii*) D.A. is given under the terms of employment; or

(*iv*) Dearness pay,

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It is treated as part of salary for certain purposes such as provident fund, value of rent free house, house rent allowance, bonus, gratuity, leave encashment etc.

Illustration 4. X receives salary of Rs. 4,000 p.m. and D.A. @ Rs. 1,000 p.m. His employer declares half of D.A. as pay (*i.e.*, enters into pay for service benefits). Compute his salary.

Solution. His salary shall be computed as under:

	Rs.	Rs.
Salary @ Rs. 4,000 p.m.	48,000	
D.A. (which enters into pay for service benefits)	6,000	
		54,000
Rest of D.A.		6,000

For all practical purposes salary of Mr. X shall be Rs. 54,000 and not Rs. 48,000.

Q. No. 4

Compute gross salary from information given below:

(*i*) Salary @ Rs. 5,000 p.m.

(*ii*) D.A. @ Rs. 1,000 p.m. [Rs. 500 p.m. enters into pay for service benefits]

(*iii*) Advance salary for two months Rs. 11,000.

(*iv*) Employer's contribution to R.P.F. Rs. 600 p.m.

[**Hints:** Gross salary Rs. 83,600]

2. City/Capital compensatory Allowance. These are given to compensate for the high cost of living in a particular big city of India or any other capital city. These are also fully taxable.

3. Lunch/Tiffin/Marriage/Family/Deputation/Wardenship/Non-practising/ Project/Overtime/Fixed Medical Allowance. These allowances are fully taxable.

4. Entertainment Allowance. It is fully taxable irrespective of the fact that any amount is spent for entertainment of the guests or customers of the employer. In some cases an employee may be eligible for deduction u/s16 (ii) which is dealt with under deduction u/s 16.

This deduction u/s 16(ii) has to be dealt with at this place because value of rent free house cannot be calculated without understanding this deduction. This deduction is to be allowed only if employee is getting entertainment allowance and this deduction is to be allowed only out of gross salary.

In case of Government employees. This deduction is to be allowed at the rate of least of following :

(*i*) Statutory Limit Rs. 5,000 p.a.

(*ii*) 1/5th of Basic Salary

(*iii*) Actual Entertainment Allowance received.

In case of other employees (i.e All non-govt employees). This deduction is to be allowed only if following two conditions are fulfilled :

(*a*) The employee is getting entertainment allowance since before 1.4.1955 ; and

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(*b*) He is working under same employer since before 1.4.1955.

In case employee fails to fulfil any of the above conditions i.e. he has joined service after 1.4.1955 or he has started getting entertainment allowance on or after 1.4.1955 this deduction will not be allowed.

The deduction will be allowed at the rate of least of following :

(*i*) Statutory Limit ; Rs. 7,500 p.a.

(*ii*) 1/5th of Basic Salary;

(*iii*) Actual Amount of entertainment allowance received at present;

(*iv*) Amount of entertainment allowance received during 1954-55 or before 1.4.1955.

C. Partially Taxable Allowances

1. House Rent Allowance

(*a*) *Employees living in hired (rented) houses.* Sometimes the employer does not provide rent-free accommodation but instead makes a provision to pay some amount in cash, so that the employee may be compensated to some extent as far as rent is concerned. The amount of cash paid is known as House Rent Allowance. Out of the total H.R.A. received, an amount equal to the minimum of the following three items is exempted from tax u/s 10(13A) read with Rule 2A and balance, if any, will be added in the salary of the employee for tax purpose. The three items are:

(*i*) 50% of salary in case of Bombay, Calcutta, Delhi and Madras, and 40% of salary in case of all other cities, or

(*ii*) Actual House Rent Allowance received; or

(*iii*) The amount by which the actual rent paid by the employee exceeds 10% of his salary, ('Salary' for this purpose includes Commission received on individual turnover basis, D.P. or D.A. if the terms of employment so provide but excludes all other allowances and perquisites).

This exemption shall be available even if employee is living in a rented house at a place other than the place of employment.

(*b*) *Employees living in their own houses or in such houses for which they are not paying any rent.* House rent allowance received is fully taxable and no portion of it is exempted under any provision of law.

(*c*) *House Rent Allowance received by Judges of High Court and Supreme Court.*

Any amount received by them is fully exempted under High Court Judges (Conditions of service) Act 1954 and Supreme Court Judges (Conditions of service) Act 1958.

Important Note. (*i*) For computation of exempted H.R.A. salary includes pay plus dearness pay or that portion of D.A. which enters into pay for service benefits.

(*ii*) In case commission is given to an employee and it is based upon turnover achieved by such employee, such commission shall also be treated as part of the salary for House Rent Allowance *[Gestener Duplicators (P) Ltd. v. C.I.T. (1979) SC)]*.

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Illustration 5. Mr. Y is employed at Amritsar on a salary of Rs. 3,000 p.m. The employer is paying H.R.A. of Rs. 350 p.m. but the actual rent paid by him (employee) is Rs. 500 p.m. He is also getting 2% Commission on turnover achieved by him and turnover is Rs. 1,50,000.

Calculate his gross salary.

Solution. *Computation of gross salary of Mr. Y*

	Rs.	Rs.
Salary @ Rs. 3,000 p.m.		36,000
Commission @ 2% of turnover		3,000
House Rent Allowance received	4,200	
Less: Exempted u/s 10(13A) (See Note 1)	2,100	
Taxable H.R.A.		2,100
Gross Salary		41,100

Note 1. Exemption of H.R.A. u/s 10(13A) read with rule 2A upto least of the following:

	Rs.	
(*i*) Actual H.R.A. received	4,200	
(*ii*) Excess of rent paid over 10% of salary (6,000 – 3,900)	2,100	(Least)
(*iii*) 40% of salary (Amritsar)	15,600	

Exempted H.R.A. = Rs. 2,100

Q. No. 5

Compute gross salary from information given below for each situation separately:

(*i*) Salary @ Rs. 3,500 p.m.
(*ii*) D.A. @ Rs. 1,000 p.m.
(*iii*) C.C.A. @ Rs. 200 p.m.
(*iv*) House Rent Allowance @ Rs. 1,000 p.m.
(*v*) Commission on turnover achieved by him is Rs. 6,000.
Situation (*a*) living in own house
(*b*) Living in rented house at Delhi as D.A. enters into pay for service benefits and rent paid is Rs. 1,500 p.m.
(*c*) Living in rented house at Chandigarh and D.A. does not enter into pay for service benefits and rent paid is Rs. 1,000 p.m.

[**Hints.** Situation (*a*) gross salary Rs. 74,400 (*b*) Rs. 62,400 (*c*) Rs. 67,200]

2. Allowances covered u/s 10 (14). Following are the prescribed allowances for the purpose of section 10(14) and their respective treatment in computing the income under the head Salaries :— [Notification No. 9807 Dated 7.7.1995.]

(*i*) *Helper Allowance.* It is exempted upto actual amount spent on engaging a helper required to perform the official duties.

(*ii*) *Uniform Allowance.* It is also exempted upto actual expenditure incurred on acquiring or maintaining of the official uniform. Excess, if any, will be taxable.

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(iii) *Academic Research Allowance.* It is exempted upto actual expenditure incurred for research. Excess, if any, is taxable.

(iv) *Conveyance Allowance.* It is exempted upto actual expenditure incurred in performance of official duties. In case amount received is more than actual expenditure, excess, if any, will be taxable.

(v) *Travelling Allowance.* It is also exempted upto actual expenditure incurred for the purposes of employment. Excess, if any, will be taxable.

Any allowance (by whatever name it may be called) granted to meet the cost of travel on tour or on transfer shall be exempted. Any allowance whether granted to employee (while on tour or for the period of journey in connection with transfer) to meet the ordinary daily charges incurred by such employee on account of absence from his normal place of employment shall also be exempted.

Such allowance shall include any sum paid in connection with transfer, packing and transportation of personal effects on such transfer.

(vi) *Any Special Compensatory Allowance in the nature of Composite Hill Compensatory Allowance or High Altitude Allowance or Uncongenial Climate Allowance or Snow Bound Area Allowance or Avlanche Allowance.*

These allowances are exempted upto different amounts in different areas as given in the notification given at the end of this chapter. In Siachen area of Jammu & Kashmir it is exempted upto Rs. 1,200 p.m. At all places located at a height of 1,000 meters or more above sea level except mentioned other-wise it is exempted upto Rs. 150 p.m. At other specified places (see notification) it is exempted upto Rs. 600 p.m.

(*vii*) *Any Special Compensatory Allowance in the nature of border area allowance or remote area allowance or difficult area allowance or disturbed area allowance.*

These allowances are exempted upto limits specified in the notification. These limits are different for different areas. These are:

(*a*) At places mentioned at point I of the notification..... ... .Exempted upto Rs. 650 p.m.

(*b*) Installations in the Continental Shelf of India and Exclusive Economic Zone of India.....Exempted upto Rs. 1,100 p.m.

(*c*) Places mentioned at point III of the notification..... .....Exempted upto Rs. 525 p.m.

(*d*) At places mentioned at point IV of the notification..... .....Exempted upto Rs. 375 p.m.

(*e*) At places mentioned at point V of the notification..... ....Exempted upto Rs. 300 p.m.

(*f*) At places mentioned at point VI of the notification..... .....Exempted upto Rs. 100 p.m.

(*viii*) *Tribal Area Allowance.* This allowance is exempted upto Rs. 100 p.m. in the States of Madhya Pradesh, Tamil Nadu, Uttar Pradesh, Karnataka, Tripura, Assam, West Bengal, Bihar and Orissa.

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(*ix*) *Any Running Allowance.* granted to an employee of transport system to meet his personal expenditure during the duty performed in the course of running of such transport from one place to another place provided that such employee is not in receipt of daily allowance.....it is exempted upto 70% of such allowance or Rs. 3,000 p.m. whichever is less.

(*x*) *Children Education Allowance.* If any amount is given by employer to employee as education allowance for the education of own children in India, it shall be exempted upto Rs. 50 p.m. per child for two children only.

(*xi*) *Hostel Expenditure Allowance.* Any allowance granted by employer to meet the hostel expenditure of employees' children it shall be exempted upto Rs. 150 p.m. for per child maximum for two children only.

(*xii*) *Compensatory Field Area Allowance.* It is exempted upto Rs. 975 p.m. in notified areas (See notification).

(*xiii*) *Compensatory Modified Field Area Allowance.* It is exempted upto Rs. 375 p.m. in notified areas as mentioned in the notification.

(*xiv*) *Any Special Allowance.* In the nature of counter insurgency allowance given to the members of the armed forces operating in areas away from their permanent locations for a period of more than 30 days shall be exempted upto Rs. 975 p.m.

MEANING OF SALARY FOR DIFFERENT PURPOSES

1. For H.R.A./PF/Gratuity and Leave encashment	Pay + D.P. + D.A. (which enters) + Commission on turnover achieved by him
2. For specified cases	All what he gets in cash less exemptions, if any, less deductions u/s 16, must be more than Rs. 24,000
3. For deduction u/s 16(ii)	Only Basic Salary
4. For gratuity under Payment of Gratuity Act	Pay + Full D.A.
5. For rent free house	Pay + D.P + D.A. (which enters) + any fee, commission or bonus (except gratutious bonus) + All fully taxable allowances + Taxable portion of other allowances + Taxable E.A. [E.A. received-deduction u/s 16(ii)] + professional tax/income tax of employee if paid by employer.

PERQUISITES [Section 17(2)]

U/s 17(1) 'Salary' includes the value of any perquisite allowed or amenity provided by employer to employee. The world 'perquisite' has not been defined under Income-tax Act 1961. Perquisite simply means any casual emolument attached to an office. Oxford English Dictionary also defines *perquisite as "any casual emolument, fee or profit attached to an office or position, in addition to salary or wages"*. Perquisites may be given in a variety of forms. If the perquisite does not accrue to the employee it will not be taxable. [*Barclays Bank Ltd. v. Naylor 39 (T.C.) 256*]. They may be received in cash or in kind. For income-tax purposes it is immaterial

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whether the perquisites are paid voluntarily or under a contractual obligation. Where goods are presented to an employee, the value to be taxed is not their cost to the employer but their value to the employee as discussed later. *[Wilkins v. Ragersion (1963) 49 I.T.R. 1395 (C.I.A.)].*

Under section 17(2) perquisites are of the following types:

(*i*) *the value of rent-free accommodation provided to the assessee by his employer;*

(*ii*) *the value of any concession in the matter of rent respecting any accommodation provided to the assessee by his employer;*

(*iii*) *the value of any benefit or amenity granted or provided free of cost or at concessional rate in any of the following cases:*

(*a*) *by a company to an employee who is a director thereof;*

(*b*) *by a company to an employee being a person who has a substantial interest in the company;*

(*c*) *by any employer (including a company to an employee to whom the provisions of section 17(2)(iii)(a) and (b) do not apply and whose income under the head "Salaries", exclusive of the value of all benefits or amenities not provided for by way of monetary payment, exceeds Rs. 24,000.*

"For the removal of doubts, it is hereby declared that the use of any vehicle provided by a company or an employer for journey by the assessee from his residence to his office or other place of work or from such office or place to his residence, shall not be regarded as a benefit or amenity granted or provided to him free of cost or at concessional rate for purposes of this sub-clause."

(*iv*) *any sum paid by the employer in respect of any obligation which, but for such payment would have been payable by the employee [Employee's electricity bill paid by the employer];*

(*v*) *any sum payable by the employer, whether directly through a fund, other than a recognised provident fund or an approved superannuation fund to effect an assurance on the life of the assessee or to effect a contract for an annuity.*

'Provided' that nothing in his clause shall apply to—

(*i*) *the value of any medical treatment provided to an employee or any member of his family in any hospital maintained by the employer;*

(*ii*) *any sum paid by the employer in respect of any expenditure actually incured by the employee on his medical treatment or of any member of his family—*

(*a*) *in any hospital maintained by the Government or any local authority or any other hospital approved by the Government for the purposes of medical treatment of its employees;*

(*b*) *in respect of the prescribed diseases or ailments, in any hospital approved by the Chief Commissioner having regard to the prescribed guidelines;*

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Provided that, in a case falling in sub-clause (b), the employee shall attach with his return of income a certificate from the hospital specifying the disease or ailment for which medical treatment was required and the receipt for the amount paid to the hospital

(Replaced by the Finance Act 1994)

(iii) *any portion of the premium paid by an employer in relation to an employee, to effect or to keep in force an insurance on the health of such employee under any scheme approved by the Central Government for the purposes of clause (ib) of sub-section (1) of section 36;*

(iv) *any sum paid by the employer in respect of any premium paid by the employee to effect or to keep in force an insurance on his health or the health of any member of his family under any scheme approved by the Central Government for the purposes of section 80D;*

(v) *any sum paid by the employer in respect of any expenditure actually incurred by the employee on his medical treatment or treatment of any member of his family [other than the treatment referred to in clauses (i) and (ii)]; so, however, that such sum does not exceed ten thousand rupees, in the previous year.*

(vi) *any expenditure incurred by the employer on—*

(1) medical treatment of the employee, or any member of the family of such employee, outside India;

(2) travel or stay abroad of the employee or any member of the family of such employee for medical treatment;

(3) travel and stay abroad of one attendant who accompanies the patient in connection with such treatment.

subject to the condition that the expenditure on travel referred to in sub-clauses (2) and (3) of this clause shall be excluded from perquisite only in the case of an employee whose gross total income, as computed before including therein the said expenditure, does not exceed Rs. Two lakhs.

(vii) *any sum paid by the employer in respect of any expenditure actually incurred by the employee for any of the purposes specified in clause (vi) subject to the conditions specified in or under that clause.*

Explanation: For the purposes of clause (2)—

(i) *"hospital" includes a dispensary or a clinic; or a nursing home*

(ii) *"family", in relation to an individual, shall have the same meaning as in clause (5) of section 10; and*

(iii) *"gross total income" shall have the same meaning as in clause (5) of section 80B;*

The value of all perquisites is included in the total income of an employee under the head 'Salary'. On the basis of above definition, *the perquisites can be divided into three categories:*

(i) Exempted perquisites.
(ii) Perquisites—Taxable in all cases.
(iii) Perquisites—Taxable in specified cases only.

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TYPES OF PERQUISITES

I *Exempted in all cases*	*II* *Taxable for all employees*	*III* *Taxable for employees covered u/s 17 (2) (iii) i.e. specified cases*
1. Free Medical facilities	1. Rent free house	1. Free use of Motor Car
2. Free refreshments	2. Concessional Rent House	2. Free gas, light, water
3. Free recreational facilities	3. Obligation of employee met by employer	3. Free Education
4. Free meals given to all employees	4. Life Insurance on the life of employee or any member of his family paid by employer	4. Free Transport
5. Free Telephone facilities		5. Free Lodging and Boarding to hotel employees
6. Free transport, Electricity gas, water etc.		6. Shares allotted to employees
7. Free refresher course, higher education or training		7. Free servants
8. Rent free house and free conveyance to judges if High Court and Supreme Court		8. Free use of heater geyser. A.C. etc.
9. Goods sold at concessional rate		9. Free Holiday home facility
10. Free ration to members of armed forces		10. Sale of assets to employee at concessional rate
11. Privilege passes to railway employees		11. Any other benefit.
12. Perks-allowed by govt. to its employees posted abroad		
13. Expenses incurred on promotion of family planning		
14. Rent free house to Union Ministers etc.		
15. Free conveyance to and fro place of employment.		

Unauthorised use of facilities by an employee

The Madras High Court in CIT vs. C. Kulandaivelu Konar (1975) 100 ITR 629 has held that "there could be no doubt that in order to bring a benefit or advantage within the provision of section 17(2) (*iii*), it must have a legal origin and since any unauthorised advantage taken by an employee without the authority of the employer would create a legal obligation to restore such advantage, it would not amount to a benefit or advantage within the meaning of section 17(2) (*iii*). The same view has been held in several other cases. As such any unauthorised benefit derived by an employee can not be treated as perquisite.

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(*i*) EXEMPTED PERQUISITES

According to the instructions from the Central Board of Direct Taxes, the following are tax-free perquisites:

1. *Medical facilities to the employees.* By amendment made by the Finance (2) Act 1991 the benefit of medical facilities is not to be treated as perquisite upto limits and rules given below:
   - (*a*) The value of any treatment of an employee or any member of his family shall be fully exempted if treatment is provided in any hospital maintained by employer.
   - (*b*) Any reimbursement of actual expenditure incurred by employee on treatment of himself or any member of his family shall be fully exempted provided the treatment is taken from a hospital maintained by local authority, a Government or any hospital approved by the Central Government.

     Any sum paid by employer in respect of any expenditure incurred for treatment of the prescribed diseases or ailments of the employee or any member of his family shall also be fully exempted.
   - (*c*) Any health insurance premium paid by employer in respect of health of employees provided such scheme is approved by the Central Govt. under section 36(1(*b*) of the Act shall also be fully exempted.
   - (*d*) Any health insurance premium paid by employee (which qualifies for deduction u/s 80 D of the Act) but reimbursed by employer shall also be fully exempted.
   - (*e*) In any other case [not covered in (*a*) and (*b*) above], any sum paid by employer to employee or reimbursement of medical expenditure incurred by him shall be exempted upto a sum of Rs. 10,000 p.a. only. Excess shall be taxable.
   - (*f*) any amount of expenditure incurred by employer or any sum paid as reimbursement of expenditure incurred by employee, in respect of
     - (*a*) medical treatment of employee or any member of his family outside India;
     - (*b*) travel or stay abroad of the employee or any member of his family for medical treatment;
     - (*c*) travel or stay abroad of one attendant who accompanies the patient (as per above) shall be exempted upto an amount permitted by RBI

       The expenditure on travel shall be exempted only in the case of an employee whose gross total income, before including this expenditure does not exceed Rs. 2 lakhs.

       The word 'Hospital' shall include a dispensary, clinic or a nursing home.
2. *Free refreshment* supplied by the employer to the employee during office hours in office premises except lunch.
3. *Recreational facilities* provided to the employee by the employer.

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4. *Free Meals*. This facility is fully exempted if given to all employees free of cost or at subsidised rate.
5. *Payment of telephone bills* by the employer for telephone installed at the residence of employee to facilitate the business of the employer.
6. *Free transport, light, water*, education or any other such service which is provided by employer from its own resources.
7. *Cost of refresher course* attended by employee met by employer. In case employer meets expenditure on higher education or training whether in India or abroad, it is fully exempted.
8. *Any rent-free residential accommodation* provided to the High Court or the Supreme Court Judges.
9. *Goods sold* by an employer to his employees at concessional rate.
10. *Free ration* received by members of armed forces.
11. *Privilege passes* and privilege ticket orders given by railways.
12. *Perquisites allowed* by Govt. to its employees posted abroad.
13. *Rent Free house given* to an officer of Parliament, a Union Minister, and leader of opposition in Parliament.
14. Conveyance facilities to Judges of Supreme Court and High Court.
15. Free conveyance provided by employer to employees for going to or coming from place of employment.
16. Any expenditure incurred by employer on promotion of family planning amongst its employees.
17. Any amount contributed by employer towards Pension or deferred annuity scheme.
18. Employer's contribution to staff group insurance scheme.
19. Accident insurance premium paid by employer for his own benefit. In case such premium is paid for an insurance whose benefit is to accuse to the employee it will be taxable.
20. Scholarships paid by employer to the children of employees.
21. Interest free loan given by employer to employee for construction of house or any other purpose cannot be treated as perk [*Krishnamurthly (P) vs. C.I.T. (1995) 126 CTR 434 (Kar.); C.I.T. vs. Vaidya M. K. (1995) 126 CTR 420 (Kar.)*]

(*ii*) PERQUISITES—TAXABLE IN ALL CASES

1. Rent-free accommodation u/s 17(2)(i)

The value of rent-free accommodation is taxable in all cases of employees irrespective of their status or salary. He may be or may not be covered by specified cases as given in 17(2)(iii) above. In a case *Lakshmipat Singhania* v. *C.I.T. (1974) 93 I.T.R. 162 it was* held that where a director is provided with rent-free accommodation, he is assessable in respect of the value thereof.

Employee's house hired by employer—provided the same free of rent. In case house belonging to an employee is hired by his employer and it is provided as rent-free house to him—the value of such house is a taxable perquisite u/s 17(2)(i) and

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rent of house received by employee from his employer shall be taxable in his hands under the head "Income from House property" u/s 22 as let out house.

Valuation of Rent Free House

For the valuation of rent-free accommodation the employees have been classified into three categories and valuation method differs from category to category. In each case valuation is made as follows:

(A) **In case of Government (Central or State) employees.** The value of rent-free accommodation (in case it is unfurnished) will be the rent which has been determined as payable by such person or officer in accordance with the rules framed by Government for allotment of residence to its officers. This category also included such Government employees whose services have been let-out to other undertakings or bodies working under the control of Government. In case of furnished house the above-mentioned value will be increased by 10% of original cost of furnishing or actual hire charges in case furniture is hired.

Mr. Aggarwal has been provided with a rent-free house. The rent of the house as fixed by the Government is Rs. 80 p.m. and salary of Mr. Aggarwal is Rs. 1,400 p.m. In this case the value of the house shall be Rs. 80 p.m. *i.e.*, Rs. 960 which will be added in salary income of Mr. Aggarwal.

(B) **In case of Semi-Government or Public sector employees.** Semi-Govt. employees are the employees of Reserve Bank of India, or of a corporation established by a Central or State Act, or of a society registered under the Societies Registration Act, 1960 and the society is financed wholly or mainly by the Government or of a company in which not less than 40% of shares are held by Central or State Government or by R.B.I. The value of accommodation in case of those employees will be:

(*i*) *If the accommodation is unfurnished*—10% of Salary (as defined later) due to such employee or Fair Rental Value whichever is less. [Notification No. 659(E), dated 15.9.86].

(*ii*) *If the accommodation is furnished*—10% of the salary due to such employee or Fair Rental Value of the house whichever is less plus 10% p.a. of the original cost of the furniture and if the furniture is hired from a third party then 10% of salary plus such hiring charges. The word 'salary' will have the same meaning as assigned to it later on.

(C) **In case of other employees (Employees in private sector including Hotel and plantation employees).**

(*i*) *Unfurnished accommodation in all towns except Bombay, Calcutta, Madras and Delhi.* Value of perquisite shall be 10% of salary (as defined later) plus the excess of fair rental value over 50% of salary.

(*ii*) *Unfurnished accommodation in Bombay, Delhi, Calcutta and Madras.* Value of perquisite shall be 10% of salary *plus* excess of Fair Rental Value over 60% of salary.

In a case where the assessee claims and the I.T.O. is satisfied that the F.R.V. of the accommodation is less than 10% of the salary of that employee, the value of rent-free accommodation shall be equal to the F.R.V. of that accommodation.

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Fair Rental Value (F.R.V.)—Defined: fair rent of a house shall be higher of following two items:

(1) Municipal valuation of that house.

(2) The rent which can be recovered from a similar type of house situated in similar type of locality or in the same locality. In case any expenditure is incurred by employer on maintenance of house or swimming pool etc. on house owned by it, such expenditure shall be added to the fair rental value of the house. (Circular no. 122 dated 19.10.1973)

Illustration 6. Mr. A gets a salary of Rs. 2,000 p.m. and is provided with rent-free unfurnished accommodation whose fair rental value is Rs. 1,300 p.m. Calculate the value of rent-free accommodation.

Solution

	Rs.	Rs.
Salary @ Rs. 2,000 p.m.		24,000
Value of perquisite: Rent-free unfurnished accommodation		
10% of salary	2,400	
+ Excess of fair rental value over 50% of salary, (Rs. 15,600 – 12,000)	3,600	
		6,000
Gross Salary		30,000

Salary—Defined. The word 'salary' for the purpose of calculating the value of rent-free accommodation *will include* pay (basic), dearness pay, fees, commission, bonus, taxable portion of an allowance or allowances payable monthly or otherwise and Income-tax and Professional tax paid or reimbursed by employer.

As per circular issued by CBDT No. 33/50/65—IT(B) Dated 27.4.66 "the amount reimbursed by way of income-tax or profession tax by the employer to employee forms part of the profits derived from the employment and is thus 'salary' for the purpose of Rule-3 of the Income-tax Rules 1962." The same view has been held by Madras High Court in a case *C.I.T. v. I.G. Mackintosh (1976) 99 (I.T.R.) 419 (Madras).*

Reimbursement of gas and electricity charges by employer, is taxable as perquisite under section 17(2)(iv) of the Act but in a case *C.I.T. v. C.W. Steel (1972). 10 I.T.R. (821),* it has been held that this amount will also be included in the term 'Salary' for calculation of value of rent-free house. But there is no Govt. notification or circular to support this view as is given in case of income-tax or professional tax paid by employer.

Even the Govt. has not included gas and electricity bill paid by employer in salary for calculation of rent-free house [See Circular Issued u/s 192 Annexure III, Illustration III Item No. 8].

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But it does not include the following:

(*i*) Dearness Allowance (D.A.) or high cost of living allowance unless it enters into retirement benefits or for computation of superannuation benefits.

(*ii*) Employer's contribution to the provident fund account of the assessee.

(*iii*) Allowance or allowances which are exempted from tax.

(*iv*) Value of perquisites like car, provision of the services of a servant, gardener, free transportation etc.

(*v*) Any advance salary or arrears of salary received.

As far as taxable portion of an allowance or allowances is concerned, it is to be noted that where an allowance is fully exempt—the same is not to be included in salary, but if a portion of an allowance is exempted or is allowed as deduction [Entertainment Allowance—deduction u/s [16(ii)] any portion which is not so exempted or allowed as deduction must be added in 'salary' for the calculation of value of rent-free accommodation.

Employee working with more than one employer simultaneously and getting rent free house from only one of them. While calculating the value of rent free house in above case, **the aggregate of salary due from both employers shall be taken into account.** [*C.I.T. vs. Mohan Lal Jalan (1989) 176 ITR 478*]

(*iii*) *Furnished accommodation.* Value of perquisite will be the amount calculated in the aforesaid manner as if the accommodation is unfurnished plus 10% of original cost of furniture or the actual hiring charges of furniture.

Furniture means normal items of furniture like soffas, chairs, curtains etc. and also includes television sets, radio sets, refrigerators, air-conditioning plant or equipment and such other household appliances.

In case furniture is hired by employer actual rent of furniture is taxable and is added to the value of rent-free unfurnished house.

Illustration 7. Mr. Z gets a salary of Rs. 3,000 p.m. and he has been provided with rent-free furnished accommodation. The fair rental value of the unfurnished house is Rs. 20,000 p.a. The cost of furnishing of the house is Rs. 30,000.

Solution

		Rs.	Rs.
Salary for the year			36,000
Value of rent-free house			
	10% of salary	3,600	
Add:	F.R.V. (–) 50% of salary (20,000 – 18,000)	2,000	
	Value of Unfurnished House	5,600	
Add:	10% of Cost of furnishing	3,000	
	Value of house (Furnished)		8,600
	Gross salary		44,600

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Illustration 8. Mr. A.B. Sen has furnished following particulars:

(*i*) Salary @ Rs. 3,000 p.m.
(*ii*) Dearness Allowance @ Rs. 500 p.m. (It enters into pay for service benefits).
(*iii*) Entertainment Allowance @ Rs. 600 p.m. (Before 1.4.55 he was getting Rs. 300 p.m. from his present employer)
(*iv*) Bonus 20% of salary.
(*v*) Salary of gardener Rs. 1,200 p.a.
(*vi*) Cost of furnishing Rs. 20,000.

Calculate the value of rent-free house if—

Case I— Mr. A.B. Sen is Govt. employee and rent of house fixed by Govt. is Rs. 300 p.m.

Case II— Mr. A.B. Sen is working in a semi-Govt. undertaking and Fair Rental Value of the house is Rs. 1,000 p.m.

Case III— Mr. A.B. Sen is working in private sector at Chandigarh and Fair Rental Value of the house owned by employer is Rs. 3,000 p.m.

Case IV— Mr. A.B. Sen is working in private sector at Delhi and Rental Value of the house not owned by employer is Rs. 3,000 p.m.

Solution. *Calculation of value of rent-free accommodation*

		Rs.
Case I.	*Govt. employee.* The value of perquisite of rent-free house is the rent fixed by Govt. for such house, which in the present case is	3,600
	Add: 10% of cost of furnishing (10/100 × 20,000)	2,000
	Value of Rent-free Furnished House	5,600

Case II. *Semi-Govt. Employee.* The value of rent-free house is 10% of *salary* or Fair Rental Value of house whichever is less.

F.R.V. (Rs. 1,000 p.m.) = Rs. 12,000 + gardener's salary Rs. 1,200
= Rs. 13,200

10% of *Salary* (Note-2) = Rs. 5,400 whichever is less is taxable value		5,400
Add: 10% of cost of furnishing (20,000 × 10%)		2,000
Value of Rent Free Furnished House		7,400

Case III. *Other employee:* The value of perquisite of rent-free house is 10% of *salary* + (F.R.V. + gardener's salary) – 50% of *salary* as town is Chandigarh) F.R.V. = Rs. 36,000 + gardener's salary Rs. 1,200 = 37,200

10% of *salary*	Rs. 5,400	
Add: Excess of F.R.V. over 50% of salary (37,200 – 27,000)		10,200

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		15,600
Add: 10% of cost of furnishing (10% of Rs. 20,000)		2,000
Value of Rent-free Furnished House		17,600

Case IV. *Other employee.* Town: Delhi, House not owned by employer. Hence, gardener's salary will not be added in F.R.V. It will be fully taxable u/s 17(2)(iii)

10% of salary	Rs. 5,400	
Add: Excess of F.R.V. over 60% of salary (36,000 – 32,400) =	Rs. 3,600	
		9,000
Add: 10% of cost of furnishing (10% of 20,000)		2,000
Value of Rent-free Furnished House		11,000

Note 1. *Deduction of E.A. u/s 16(ii)*

Least of following is allowed as deduction:

(*i*)	Rs. 7,500 p.a. St. limit	
(*ii*)	1/5th of salary (36,000)	Rs. 7,200 ✓
(*iii*)	Actual E.A. received	Rs. 7,200 ✓
(*iv*)	E.A. before 1.4.55	Rs. 3,600 (least)

Hence Taxable E.A. = 7,200 (–) 3,600 = 3,600

Note 2. *Salary of the employee for the calculation of value of rent-free House*

	Rs.
Salary	36,000 ✓
D.A. (which enters)	6,000 ✓
Bonus 20% of salary (Pay+D.A)	8,400 ✓
Taxable E.A. (Note—1)	3,600 ✓
	54,000

2. Concessional Rent Accommodation u/s 17(2)(ii)

If the accommodation is provided at a concessional rent, then the value of the concessional accommodation is to be included in employee's salary. The value of the concession will be the amount by which the rent-free accommodation value [as calculated in the non-concessional case] exceeds the rent paid by the employee. For example, the employee pays a rent of Rs. 100 p.m. to his employer for the accommodation the value of which is Rs. 2,000 p.a.

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In case the rent-free value exceeds the rent paid by (Rs. 2,000 – 1,200 = Rs. 800). So, the value of concessional accommodation will be Rs. 800.

Illustration 9. Mr. Ravinder is in receipt of annual salary of Rs. 20,000. He is provided with a furnished accommodation for which his employer pays a rent of Rs. 14,400 p.a. and deducts Rs. 200 p.m. from employee's salary. The cost of furnishing of the residence amounts to Rs. 30,000. Calculate the value of perquisites.

Solution

		Rs.	Rs.
	Salary for this purpose		20,000
	Value of perquisite		
	10% of salary	2,000	
Add:	Excess of F.R.V. over 50% of salary (Rs. 14,400 – 10,000)	4,400	
	Value of Unfurnished Accommodation	6,400	
Add:	10% of cost of furniture (10% of Rs. 30,000)	3,000	
		9,400	
Less.	Rent paid by the employee @ Rs. 200 p.m.	2,400	
	Value of Concessional accommodation		7,000

Illustration 10. Mr. B.P. Yadav was serving as Chief Accountant in a private sector company at Calcutta. He was staying in a house provided to him free by the company and the fair rental value of the same was Rs.5,000/- p.m. His salary particulars are as follows :

	Rs.
Salary	6,000/- p.m.
D.A.	400/- p.m.
Educational allowance (2 children)	300/- p.m.
Conveyance allowance	600/- p.m.

Mr. yadav spends Rs. 500/- p.m. towards conveyance for official duties.

He was also doing over-time work for which he was getting a salary of Rs. 1,000/- p.m.

On 1-10-96 Government of India took over the company but he continued to stay in the house and drew the same salary and allowances. He however, left the part time job. On 28th February 1997, he resigned from the company and joined a private company on 1-3-97 which gave him a rent free house. The fair market value of the same is Rs. 5,000/- p.m. But the standard rent under the Rent Control Act is Rs. 3,000/- p.m. The company gave him a gross salary of Rs. 12,000/- p.m.

Determine the perquisite value of residential house occupied by Mr. Yadav.

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Will your answer be different if during occupation of the house as a public sector employee he pays to the company a rent of Rs. 400/- p.m. fixed as a standard rent payable by him as per the rules of the company ? In all the above cases salary was due on last date of month.

Solution. *Calculation of Value of rent free house*

A. Private Sector Employee [1.4.96 to 30.9.96]

(*a*)	*Salary for rent free house (six months)*		
	Salary		36,000
	D.A. not to be included as it does not enter into pay for service benefits		NIL
	Education Allowance [300 × 6]	Rs. 1,800	
Less :	Exempted [50 × 2 × 6]	Rs. 600	
			1200
	Conveyance Allowance	Rs. 3,600	
Less :	Spent for duties	Rs. 3,000	
			600
	Salary for overtime		6,000
			43,800
(*b*)	*Fair Rental value of the house*		30,000
(*c*)	*Value of house*		
	10% of salary		4,380
Add :	FRV (–) 60% of salary [30,000 – 26,280]		3,720
			8,100

B. Public Sector Employee [1.10.96 to 28.2.97]

(*a*)	Salary for rent free house [36,000 + 1200 + 600] = 37,800 reduced to 5 months [37,800 × $^5/_6$]		31,500
(*b*)	F.R.V. of the house		25,000
(*c*)	Value of house		
	10% of salary	3,150	
	or		
	F.R.V.	25,000	
	w.e. is less is taxable =		3,150

C. Private Sector Employees [1.3.97 to 31.3.97]

	Salary	12,000
	F.R.V.	5,000
	10% of salary	1,200
Add :	F.R.V.—60% of salary [5,000 – 7,200]	NIL
	Value of House	1,200

Value of rent free house = Rs. 8,100 + Rs. 3,150 + Rs. 1,200
= 12,450

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In case employee pays rent fixed by employer during his job with public sector company the value of house is taken as NIL [*Officer's Association, Bhillai Steel Plant v. Union of India (1993)M.P.*]

Q. No. 6

Compute the value of benefit of house for each situation separately from particulars given below:

(*a*) Salary Rs. 5,000 p.m.

(*b*) Bonus (*i*) statutory Rs. 10,000 and (*ii*) Gratutious Rs. 5,000

(*c*) Conveyance allowance @ Rs. 400 p.m.

(*d*) Entertainment allowance @ Rs. 500 p.m.

(*e*) Arrears of salary for the previous year 1995-96 Rs. 6,000

(*f*) Cost of furnishing is Rs. 25,000 and a hired air-conditioner is provided for 6 months every year and rent paid in respect of such airconditioner is Rs. 1,000 p.m.

Situation (*i*)—Employee is a Govt. employee and rental value of the house is Rs. 400 p.m.

Situation (*ii*)—Employee is working in L.I.C. at Chandigarh. House is owned by the corporation and its Fair Rental value is Rs. 24,000 p.a. He was employed on 1.4.67.

Situation (*iii*)—Employee is working in a Public Ltd. company at Delhi and rent paid by company is Rs. 48,000 p.a. Employee pays Rs. 250 p.m. as rent. He joined service on 1.9.1953 and was getting Entertainment Allowance @ of Rs. 350 p.m. on 1.9.1953.

[**Hints.** Situation (*i*) Rs. 13,300; Situation (*ii*) Rs. 16,580; Situation (*iii*) Rs. 15,200]

Q. No. 7

P and Q are officers in the State Bank of India. The bank has allotted free of rent identical flats to both P and Q in Nariman Point Bombay, the fair market rent of each flat being Rs. 6,000/- p.m. in April '96. P was promoted as Chief officer but he continues to occupy the same flat. The Bank has also furnished the above flats. The original cost of furniture provided in each flat works out to Rs. 45,000/-. The salary particulars of P and Q are as follows :

	P	Q
	Rs.	Rs.
Basic	9,000/- p.m.	7,500/- p.m.
Dearness pay (enters)	1,750/- p.m.	1,600/- p.m.
Dearness allowance	1,500/- p.m.	1,400/- p.m.
Educational allowance	1,200/- p.m.	1,200/- p.m.
Children hostel allowance	1,500/- p.m.	1,200/- p.m.
Petrol allowance	900/- p.m.	800/- p.m.

Determine the perquisite value of the flat in the hands of P and Q. Two childrens are studying and staying in hostel in each case.

[**Hints :** Semi Govt. Employees, value of rent free house for P Rs. 21,240 and for Q Rs. 18,780]

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3. Any obligation of employee met by employer—17(2)(iv)

Any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the employee, *e.g.*, electricity bill, club bills, salary of domestic servants, salary of a gardener employed by employee, etc. if paid by employer are taxable under this provision. Cost of free medical facilities and reimbursement of medical expenses are fully exempted.

4. Insurance Premium paid by Employer—17(2)(v)

If any employer pays any premium to effect an insurance on the employee, or make a payment in respect of a contract for annuity, such payment by employer will be taxable in the hands of each such employee.

Insurance Policy acquired by the employer to get the employee insured against accidents

In case of accidents, the employer is required to pay compensation to his workers and in case employer gets life insurance policy on worker against injury or death by accidents to meet his own liability arising from such accidents, premium paid on such life policies of workers shall not be treated as a perk, in the hands of the employees.

However, insurance premium paid by the employer on life policy of an employee for the benefit of the worker shall be treated as a taxable perk in the hands of the employees u/s 17(2)(v). *[C.I.T. v. Lala Shri Dhar (1972) 84 I.T.R. 192].*

(*iii*) PERQUISITES—TAXABLE IN SPECIFIED CASES ONLY

The following perquisites are to be added in the employee's salary only if these perquisites are given to such employees who are fulfilling any of the following three conditions:

(*a*) by a company to its director employee.

(*b*) by a company to its employee who is having substantial interest in the company (substantial interest means holding not less than 20% of voting power).

(*c*) by any employer to its employee drawing a salary exceeding Rs. 24,000 p.a. (includes all monetary emoluments only).

Explanation. If the employee is not drawing a salary exceeding Rs. 24,000 or is not a director or is not having a substantial interest in the company then the following perquisites are free of tax. It means, if he is provided with the car facility, it will not be taxed.

'Salary' for the purpose of including an employee under specified cases must exceed Rs. 24,000 p.a. This is given as under u/s 17(2). "*.....whose income under the head 'salaries' (whether due from or paid or allowed by one or more employers) exclusive of the value of all benefits or amenities not provided for by way of monetary payment exceeds twenty four thousand rupees*".

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It nowhere implies that we have to take income taxable under the head salaries *i.e.*, after deductions u/s 16(i), (ii), and (iii). It simply means that the amount received by an employee from his employer in cash which comes within the scope of head 'salary'. Wheresoever law needs taxable income it clearly writes *"income chargeable to tax"* [See Income-tax Act section 22, section 28, section 32AB etc.]. Hence there is no need to deduct any amount u/s 16(i), (ii) and (iii) out of sums received by employee in cash for finding out his eligibility u/s 17(2)(iii). Although we personally still hold the above view, but keeping in view the interests of the students, the numericals in this book are being solved after allowing Standard Deduction u/s 16 (i), Entertainment Allowance u/s 16 (ii) and Professional Tax u/s 16 (iii) for the purposes of salary of Rs. 24,000.

These perquisites are:

1. Motor Car

Employer's car for employees personal use. If the employee is provided with the car facility exclusively for his personal or private use, the value of the perquisite will be the actual amount spent by the employer in providing with this facility. So it will include all maintenance, running, repairs, wear and tear expenses etc.

Employer's car for employee's official use only. As in this case, employee is using the car for his official use only and not for personal or private use it shall not be treated as perquisite because the employee is not deriving any benefit out of it.

Employer's car for employee's personal and official use. The value of a motor car provided by the employer for the use of the assessee partly for his personal use and partly in performance of his duties, shall be deemed to be the sum equal to that part of the amount actually expended by employer on the maintenance and running of the motor car during the relevant previous year (including remuneration, if any, paid by the employer to chauffeur) which can reasonably be attributed to the use of the motor car by the employee for his private or personal purposes. *However, where a determination on the basis mentioned above* presents difficulty, the value of perquisite may be determined on the basis provided in the table given below:

	Small Car (upto 16 H.P.)	*Big Car (More than 16 H.P.)*
Expenses met by Employer	600 p.m.	800 p.m.
Expenses met by Employee	200 p.m.	300 p.m.

In case where driver/chauffeur is also provided by employer, the above values shall be increased by Rs. 300 p.m. each.

Month means a complete month and a fraction of month, if any, is to be ignored.

Where employee owns a car

In case the motor car is owned by the employee but its running and maintenance expenses are met or reimbursed by the employer, the value of perquisite shall be the

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amount of such expenses as the I.T.O. may reasonably attribute for the personal or *private use* of the employee.

Use of Motor Car at concessional rates. In case the employee is provided with car at concessional rates, the value of perquisite will be the value of motor car provided free of charges *less* expenses met by employee himself.

Where more than one car is put at the disposal of employee. In case employee is allowed to use any car out of pool of cars of different sizes, one car with higher horse power shall be taxable.

Free use of any other type of conveyance. When the employee is enjoying the facility of any other type of conveyance, the reasonable expenditure incurred by the employer in providing with the free use of conveyance to the employee shall be taken as the value of the perk. So the value of the perquisite will be the amount, the employer has incurred for the *private use* of the employee.

Provision of Conveyance by employer from residence to office or vice versa [Explanation to Section 17(2)(*iii*)].

In case employer provides car or other conveyance to employee for going to the place of employment or vice versa, it will not be treated as perquisite under this section.

Illustration 11. What will be the value of car benefit provided by employer to employee in the following cases:

(*a*) Car 18 HP: Expenses met by employer. Exclusively used for employment purposes.

(*b*) Car 14 HP: Expenses met by employer Rs. 8,400 p.a. Depreciation of car Rs. 13,600 p.a. used exclusively for personal purposes by employee.

(*c*) Car 18 HP for private and official use—maintenance expenditure Rs. 16,000 p.a. Registration fee Rs. 3,000 p.a. Depreciation Rs. 12,000 p.a. Salary of driver Rs. 600 p.m. I.T.O. has accepted the contention of employee that car is used 60% for official purposes and 40% for personal purposes.

(*d*) 16 HP car for private and official use. Expenses met by employer. Chauffeur is also provided. Employer deducts Rs. 300 p.m. from employee's salary for this benefit.

Solution

(*a*) Value of benefit is Nil as car is used exclusively for official purposes.

(*b*) Value of benefit is Rs. 22,000, *i.e.*, all the expenses met by employer on such car, because car is fully used for personal purposes.

(*c*) Value of perk, is calculated in the following manner:

	Rs.
(*i*) Maintenance Expenses	16,000
(*ii*) Registration fee	3,000

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(*iii*)	Depreciation	12,000
(*iv*)	Salary of driver 600 p.m.	7,200
	Total Expenses	38,200
	Value of benefit 40% of actual expenditure (38,200 × 40/100)	15,280
(*d*)	Value of perk. will be	
	Value for 16 H.P. car as fixed in Table:	
	Exp. met by employer:	
	Rs. 600 p.m.	7,200
Add:	Driver's salary @ Rs. 300 p.m.	3,600
	Total	10,800
Less:	Amount deducted by employer @ Rs. 300 p.m.	3,600
	Taxable value	7,200

Illustration 12. Calculate the value of car facility in following cases if (*a*) P is a specified employee *i.e.*, he is (*i*) a director-employee of a company (*ii*) a substantially interested employee of a company (*iii*) employee drawing more than Rs. 24,000/- by way of monetary salary and (*b*) P is neither a director nor a shareholder and his salary does not exceed Rs. 24,000/-.

1. P uses his own car fully for official purposes. The cost of maintenance and depreciation comes to Rs. 18,000/- p.a. to his employer.
2. P uses his own car for personal purposes. He meets the petrol cost which amounted to Rs. 15,000/- and the employer bore the cost of maintenance amounting Rs. 9,000/-.
3. P uses his own car fully for private purposes. The employer reimburses the entire cost of running and maintenance amounting to Rs. 10,000/-.
4. The employer provides his own car to P for his private use. W.D.V. of the car as on 1-4-96 is Rs. 90,000/-. Rate of depreciation is 20%. The employer spends Rs. 18,200/- on running and maintenance of the car.
5. Employer provides own small car to Mr. P for his official and personal use. W.D.V. of the car as on 1-4-96 Rs. 66,000/-. Depreciation is admissible at the rate of 20%. The employer spends Rs. 12,000/- on running and maintenance and pays Rs. 9,000/- as driver's salary. However it is difficult to work out expenditure attributable towards private use of the car as the employer does not maintain any log book.
6. Employer provides a car to P for his private purposes. W.D.V. as on 1-4-96 is Rs. 102,000/-. Depreciation admissible 20%. P meets the running and maintenance cost.
7. Employer provides car to Mr. A travelling from residence to office and back from office to residence.

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8. Out of a pool of 7 motor cars (horse power rating of one of which exceeds 16) owned by the employer, Mr. P is free to use any one of them for his official as well as personal purposes. Though the employer has provided a chauffeur to Mr. P he rarely uses his services. No log book is maintained by the employer.

Solution. *Calculation of value of car for Mr. P*

Situations	*If covered under specified cases*	*If not covered under specified cases*
	Rs.	Rs.
1. Car owned by employee and used for employment purposes—expenses met by employer	No benefit	No benefit
2. Car owned by employee and used for personal purposes—expenses met by employer—Fully Taxable u/s 17(2)(*vi*) as obligation of employee	9,000	9,000
3. Reimbursement of car expenses by employer—car used only for personal purposes—fully taxable u/s 17(2)(*iv*)	10,000	10,000
4. Car owned by employer—used only for private purposes. Actual expenses met by employer are taxable only in specified cases. u/s 17(2)(*iii*) Dep. 90,000 × 20% = 18,000 Running Expenses = 18,200 36,200		NIL
5. Small car owned by employer—used partly for personal and partly for official purposes—Actual expenses cannot be apportioned hence taxable value is Rs. 600 × 12 = 7,200 Driver's salary Rs. 300 × 12 = 3,600 Taxable value is specified cases 10,800	10,800	NIL
6. Car owned by employer—used entirely for personal purposes,		

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Situations	*If covered under specified cases*	*If not covered under specified cases*
expenses met by Employee— Depreciation of car is taxable in specified cases only. [Rs.102,000 × 20% = 20,400]	20,400	NIL
7. The benefit of conveyance given by employer to employee for going to or coming from place of employment is exempted u/s 17(2) explanation	NIL	NIL
8. Only value of one car with higher horse power is taxable u/s 17(2)(*iii*) value of car [800 × 12] 9,600 Driver's salary [300 × 12] 3,600	13,200	NIL

Q. No. 8

Calculate value of the benefit of car in following cases separately:

(*i*) Car (8 H.P.) owned by employee and used for both personal and employment purposes. Employee spends Rs. 12,000 p.a. and does not get any conveyance allowance.

(*ii*) Car (18 H.P.) owned by employee and used equally for both personal and employment purposes and spends Rs. 12,000 p.a. His employer gives him conveyance allowance @ Rs. 600 p.m.

(*iii*) Car owned by employer. Expenses of Rs. 45,000 p.a. on maintenance of car are met by employer. It is accepted by Assessing Officer that car is used for 50% time for personal purposes.

(*iv*) Car of 16 H.P. provided for personal and employment use and expenses are met by employer but employee pays Rs. 200 p.m. for personal use of car.

(*v*) Car of 18 H.P. provided by employer for personal and employment purposes and expenses are met by employee. Driver is also provided and his salary paid by employer is Rs. 600 p.m.

[**Hints.** (*i*) Nil; (*ii*) Taxable conveyance allowance Rs. 1,200; (*iii*) Rs. 22,500; (*iv*) Rs. 4,800; (*v*) Rs. 7,200].

2. Free Gas, Electricity or Water Supply for Household Use

The value of perquisite is determined as under:

(*i*) Actual Bill paid by employer to an outside supplying agency: It is taxable in all cases u/s 17(2)(*iv*).

(*ii*) Where the office and residence of an employee are situated in the same building and a common bill for gas, electricity or water supply is paid by employer, the bill will be apportioned between office and residence on area basis, and the benefit accruing to employee for his residence shall be the value of perquisite which will be added in his salary.

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This benefit must not exceed $6\frac{1}{4}\%$ (1/16) of employee's salary, *i.e.*, Pay and D.A. (which enters into pay for service benefits only).

(*iii*) Where the employer provides these facilities from its own source, the value of perquisite will be taken as nil.

3. Free Education to the Members of Employee's Household

Where the employer pays for the provision of free education facility for any member of the employee's household, the value of the perquisite will be the amount incurred by the employer. In case educational institution is run by the employer, the value of perquisite to the employee will be the reasonable cost of such education in a similar institution in or near the locality.

4. Free Transport

When the employer, who is engaged in the transportation business, provides free transport facility to its employees, their family members and dependents, the value of such perquisite will be taken as nil. In case employer hires a conveyance and provides free of charge to its employees, the value of benefit taxable u/s 17(2)(iii) is the amount actually spent by employer. Where transport facility for the purpose of going from the place of work or from such place back to residence, is provided to group of employees, the value of perquisite is nil.

5. Lodging and Boarding facilities to Hotel Employees

The value of this perquisite will be as under:

Lodging. Value (as calculated above) of rent-free house or actual rent, whichever is less. This rule is applicable in case of Hotel employees and is taxable in case of every employee.

Boarding. Actual cost of boarding including overheads as per accounts prepared by the hotel.

6. Shares allotted to employees

As per circular no. 710 dated 24.7.1995 any shares issued by companies to its employees at concessional price amounts to perquisite taxable in specified cases of employees u/s 17(*iii*) in following manner :

(*a*) *Shares held by government and issued to the employees of the company.* It shall not constitute any perquisite as relationship between government and employees of the company is not that of employer and employee.

(*b*) *Shares offered by company to employees at same price as to other shareholders.* The value of benefit shall be nil.

(*c*) *Shares given to employees at price lower than the price at which given to other shareholders.* The value of perquisite shall be the difference between the price charged from shareholders and price charged from employees shall be taxable.

(*d*) *Shares given only to employees.* The difference between market price of the share and price charged from employees is taxable.

7. Treatment of Servants

(*i*) Any servant employed by employee but salary is paid by or reimbursed by employer. Full salary is taxable for all employees u/s 17 (2) (iv) as obligation of employee is met by employer.

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(*ii*) **Servants employed by employer but provided to employee or services of servants are provided by employer.** Under new rule 3(*ba*) if free services of sweeper, watchman (security) or gardener are provided by employer, these shall be taxed at Rs. 120 p.m. per person and shall be taxable only in specified cases.

(*iii*) **Other domestic servants.** Full salary is taxable in specified cases only.

Q. No. 9

Calculate the taxable value of use of servants in following cases separately:

A. Salary of gardener paid by employer Rs. 1,200 p.a. Fair Rental Value of house owned by employer is Rs. 30,000.

B. Salary of gardener, sweeper and watchman is Rs. 400 p.m., Rs. 180 p.m. and Rs. 750 p.m. respectively and they are employed by employee but their salary is paid by employer. House is owned by employee.

C. House hired by employer at the rate of Rs. 1,500 p.m. Gardener's salary is paid by employer @ Rs. 400 p.m. Salary of the employee is Rs. 60,000 p.a.

D. House owned by employer. Salary of Sweeper @ Rs. 200 p.m. and watchman @ Rs. 400 p.m. is paid by employer. Salary of the employee is Rs. 40,000 p.a.

[**Hints. A.** Gardener's salary to be added in FRV (Rs. 30,000 + Rs. 1,200 = Rs. 31,200);

B. Full salary is taxable u/s 17(2(*iv*));

C. Gardener's salary of Rs. 1,440 p.a. is fully taxable as a separate perquisite;

D. Rs. 1,440 for sweeper and Rs.1,440 for watchman]

8. Free use of Heaters, Boilers, Refrigerators etc.

If the employee has been provided the free use of these facilities and also a house by the employer, then 10% of cost of these articles is added in the value of the rent-free accommodation. But in case employee has been provided with the free use of these articles but not a free house, then 10% of the cost of these articles or hire charges is taken as taxable value of these articles under specified cases.

9. Facility of Holiday Homes etc. provided to employees

In case employer has maintained holiday homes for the use and benefit of employees, the benefits like free travelling, free boarding and lodging would be taken as a taxable perquisite in the hands of specified type of employees. While calculating taxable value of the perk, effort should be made to find out the reasonable and fair value of benefit derived by the employee taking into consideration the type of accommodation, facilities available, number of days stay and cost of similar type of accommodation available outside.

10. Sale of Assets to the Employee at Concessional Rate

In case the employee has sold certain assets at concessional price or given such assets to employees as gifts etc. the value of benefit derived by the employee shall be taxable. The value of the benefit is to be calculated by taking the difference between the sale price and the market price on the day it was sold or transferred to the employee.

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11. Miscellaneous Benefits

In case of any other perquisite, not discussed so far, the value of the same shall be determined on such basis as the Assessing Officer considers fair and reasonable. These benefits may be given to the employee or to any other member of his family. The value of the perquisite given in kind shall be calculated not by taking the cost of that asset to the employer but its value or benefit to the employee or price which the employee could have received for the same, if sold. Free meals, if given to any one employee, are also taxable for specified employees.

PROFITS IN LIEU OF SALARY [17(3)]

Profits in lieu of salary include—

(i) The amount of any compensation due to or received by an assessee from his employer or former employer at or in connection with the termination of his employment or the modification of the terms and conditions relating thereto.

(ii) Any payment (other than any payment referred to in clause (10), Clause (10A), Clause 10(B), Clause (11), Clause (12), 13 (with effect from 1-4-96) or Clause (13A) of section 10, due to or received by an assessee from an employer or a former employer or from a provident or other fund to the extent to which it does not consist of contributions by the assessee or interest on such contributions.

Receipts not included in Profit in lieu of Salary

Any payment received whether from present or past employer, is taxable as profit in lieu of salary. The following receipts, however, are exempted:

1. Leave Travel Concession [Section 10(5)]. Any amount received by an employee from his employer for proceeding on leave anywhere in India or on proceeding to any place in India after retirement is exempted upto the extent of an amount provided u/s 10(5) and rules framed thereunder.

This benefit is available to employee for self and any member of his family. The word *"family"* includes spouse and children of the individual and parents, brothers or sisters who are mainly dependent on such individual.

The exemption under this section shall be available subject to rules and regulations framed by the Central Government.

Exempted limits are—

(i) When journey is performed by rail. Exempted upto amount of air-conditioned second class fare by shortest possible route.

(ii) When journey is performed by some other mode but rail link exists. Exempted upto an amount equivalent to 2nd class Air-conditioned fare by shortest possible route.

(iii) When places are not connected by rail. First class or deluxe class bus fare by shortest possible route shall be exempted. The leave travel concession shall be available only for two journeys performed in block period of 4 years commencing on 1.1.89. In case an employee has not availed the benefit in block period but avails it in the first year of next block, exemption will be admissible in such year.

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In case benefit is given without actual expenditure, no exemption shall be allowed. It will be fully taxable.

2. Perquisites and Allowances paid by Government to its employees posted outside India [Section 10(7)].

Any perquisite or allowance given by Government to its employees who are working outside India is fully exempt from tax. As such Motor car provided to employee working outside India or house rent allowance or any other such benefit is fully exempted from tax.

3. Gratuity [Section 10(10)].

(*i*) *Death-cum-retirement gratuity*—any such amount received by the employees working in Civil or Defence services of Govt. of India, or on any post of State Govt. or Local authority covered under Revised Pension Rules of the Central Govt., shall be fully exempted.

(*ii*) *Gratuity received under Payment of Gratuity Act, 1972.* In case of employees covered by the Payment of Gratuity Act, 1972, an amount being least of following *three* items shall be exempted and excess if any, will be taxable. Three items are:

(*i*) 15 days salary (7 days in case of employees working in seasonal factories) for each year of completed service or part thereof in excess of six months.

(*ii*) Notified Limit Rs. 100,000. (During whole life)

(*iii*) Gratuity actually received by the employee.

'Salary' means salary last drawn by the employee and it also includes dearness allowance. Average salary shall be calculated by taking 26 days as the maximum number of working days in a month. For example if the employee was drawing Rs. 1,300 at the time of his retirement, then 15 days average salary shall be

$$\text{Rs. } 1{,}300 \times \frac{15}{26} = 750.$$

The Payment of Gratuity Act provides that only those employees who fulfil following conditions are covered under this Act :—

(*i*) an employe who is working in a factory covered under Factories Act ;

(*ii*) who is working on a non managerial post.

Illustration 13. Mr. Gavaskar retires from his job on 30th Nov. 1996 after putting 30 years and 7 months' service. He received Rs. 40,000 as gratuity under the Payment of Gratuity Act. His Salary including Dearness Allowance at the time of retirement was Rs. 1,950.

Solution

Least of 3 items shall be exempted

(*i*) 31 × 1,125 = Rs. 34,875 [Least]

(*ii*) Notified Limit Rs. 100,000

(*iii*) Actual amount Rs. 40,000

Taxable Gratuity shall be = 40,000 – 34,875 = 5,125

15 day's salary has been calculated as 1,950 × 15/26 = 1,125

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(*iii*) *For Other employees*—exempted upto least of following:

(*a*) Notified limit Rs. 2,50,000 (During whole life)

(*b*) 1/2 month's average salary for every one completed year of service [months to be ignored]

(*c*) Actual gratuity received.

In case gratuity is received from private employer, an amount equal to least of the above three items shall be exempted provided:

(*i*) Employee has completed at least 5 years' continuous service; or

(*ii*) He is leaving the job before the completion of 5 years not of his own, *i.e.*, he was terminated or retrenched or his service has come to an end because of reasons beyond his control.

Average salary. With effect from assessment year 1989-90 the average salary is to be computed by taking salary of last 10 months preceding the month in which retirement or death occurs.

Notified Limit. The limit of Rs. 2,50,000 is applicable for whole serving life of employee. In case gratuity is received from more than one employer the aggregate amount of gratuity received must not exceed Rs. 2,50,000.

Salary. The word 'salary' here has the same meanings as is assigned to it for provident fund purposes, *i.e.*, the Basic Pay plus dearness pay or any portion of D.A. which enters into pay for service benefits plus commission received on fixed % age of turnover achieved by him.

By amending the provisions of section 10(10) the Government has taken over the powers to raise the limits of exempted gratuity by just issuing a notification.

In the case of persons employed by Governments, Local bodies, and statutory corporations, the full amount of death-cum-retirement gratuity received by an employee is exempted from tax.

Illustration 14. Mr. Singh, the Works Manager of a company retires on 30.6.96 after putting 38 years of continuous service. He received a gratuity of Rs. 50,000 in August 1996.

His salary for the year 1995-96 was Rs. 2,500 p.m. and 1996-97 Rs. 2,600 p.m.

Calculate his exempted gratuity.

Solution

	Rs.
The average salary is calculated as below:	
Salary for April and May 96 @ Rs. 2,600 p.m.	5,200
Salary from August 95 to March 96 @ Rs. 2,500 p.m.	20,000
Salary of last 10 months	25,200

Average salary = 25,200 ÷ 10 = 2,520

Least of following shall be exempted:

(*i*) Notified Limit = Rs. 2,50,000

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(*ii*) Actual Amount received Rs. 50,000

(*iii*) $^1/_2$ month's average salary for every one completed year of service (2,520/ 2 × 38) Rs. 47,880 (Least)

Taxable = Rs. 50,000 (–) 47,880 = 2,120

Q. No. 10

Mr. Barua received Rs. 60,000 on his retirement on 30.9.96 as gratuity from his employer with whom he has served for 29 years and 7 months. Compute the taxable amount in each of the following cases separately if his salary during calender year 1995 was Rs. 2,000 and during 1996 was Rs. 2,400 and it is due on 1st of every month. He had worked earlier with a company for 6 years and received Rs. 12,000 as gratuity which was fully exempted u/s 10 (10)

A. He is Government employee;

B. He is working in a machine tool factory at Ludhiana (covered under Factories Act);

C. He is working in a commercial office at Delhi.

[**Hints.** A. Fully exempted; B. Rs. 18,462; C. Rs. 26,360]

4. Any payment received in commutation of Pension. [Section 10(10A)]. Any amount of pension received monthly or otherwise from any employer is fully taxable but any amount received in lump sum as commuted value is to be treated in the following manner:

The amount received by an employee as commuted value of pension is fully exempted if he receives it from:

(*a*) Central Government; or

(*b*) State Government; or

(*c*) Local Authority; or

(*d*) A corporation set up under Central, State or Provincial Act; under the Civil Pensions (Commutation) Rules of the Central Government; or

(*e*) as Judge of Supreme Court or High Court in India.

In case of other employees, any amount received on commutation of pension is exempted subject to following limits:

(*a*) In case where the employee receives any gratuity, the exempted amount shall be commuted value of one-third ($^1/_3$) of pension which he is normally entitled to receive.

(*b*) In case where the employee does not receive gratuity, the exempted amount shall be the commuted value of one-half ($^1/_2$) of such pension.

Illustration 15. Find out the taxability of pension in the following cases:

(*i*) Mr. Shri Kant retires from a public limited company on 31st August 1996 and his pension was fixed at Rs. 1,500 p.m. He does not commute any part of pension.

(*ii*) Mrs. R retires from Government service on 30th September, 1996 and her pension was fixed at Rs. 1,000 p.m. She does not commute any portion of pension.

(*iii*) Mr. Raju retires from Punjab Government service on 30th June, 1996 and his pension has been fixed at Rs. 1,200 p.m. He gets 1/3rd of his pension commuted for Rs. 60,000.

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(*iv*) Mr. Reddy retires from private service on 30th April, 1996 and his pension has been fixed at Rs. 1,500 p.m. He gets 1/2 of his pension commuted and gets Rs. 80,000. He also received Rs. 75,000 as gratuity. He gets his pension commuted during January, 1997.

In all cases, pension becomes payable on the 1st day of each month.

Solution

(*i*) Uncommuted pension received from private sector is fully taxable. Mr. Shri Kant's taxable pension shall be Rs. 1500 × 6 = 9,000 *i.e.*, from 1st September payable on 1st October to 31st March.

(*ii*) Uncommuted pension received by Mrs. R is fully taxable. Her taxable pension shall be Rs. 1,000 × 5 = Rs. 5,000.

(*iii*) Commuted portion of pension received by Mr. Raju *i.e.*, Rs. 60,000 is fully exempted. Uncommuted portion of pension @ Rs. 800 p.m. will be fully taxable. Mr. Raju's uncommuted portion of pension shall be Rs. 800 × 8 = Rs. 6,400 during the previous year 1996-97.

(*iv*) Commuted portion of Pension of Mr. Reddy shall be taxable as under:

For $^1/_2$ portion of pension he gets	= 80,000
For full portion of pension he gets	= 80,000 × 2
$^1/_3$rd portion of commuted pension shall be exempted	= 80,000 × $^2/_1$ × $^1/_3$
	= Rs. 53,333
Taxable portion of commuted pension shall be	= 80,000 – 53,333
	= 26,667

Uncommuted portion of pension of Rs. 1,500 × $^1/_2$ = 750 p.m. for 2 months is fully taxable. Uncommuted pension of Rs. 1,500 p.m. for 8 months (*i.e.* 1.6.96 to 1.1.97) is also fully taxable.

Illustration 16. Mr. Tejinder Singh retired on 31.12.96 and his pension was fixed at Rs. 600 p.m. He got 3/4th of the pension commuted for which he received Rs. 30,000 from his employer, a Ltd. Co. Find out the taxable amount of commuted value of pension if:

(*a*) he gets gratuity; and (*b*) he does not get gratuity.

Solution

If he gets gratuity. Exempted upto commuted value of $^1/_3$ of pension

	Rs.
For $^3/_4$ of pension commuted value is	= 30,000
For full of pension commuted value is	= 30,000 × $^4/_3$
For $^1/_3$ of pension commuted value is	= 30,000 × $^4/_3$ × $^1/_3$
Exempted	= 13,333

Taxable = Rs. 30,000 – 13,333 = Rs. 16,667

If he does not get gratuity. *Tax free upto commuted value of $^1/_2$ of pension*

	Rs.
For $^3/_4$ of pension commuted value is	= 30,000
For full of pension commuted value is	= 30,000 × $^4/_3$

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For $^1/_2$ of pension commuted value is = 30,000 × $^4/_3$ × $^1/_2$
Exempted = 20,000
Taxable 30,000 – 20,000 = 10,000.

Q. No. 11

Mr. Sen Gupta retired on 31.5.96 and his pension was fixed at Rs. 1,500 p.m. His salary at the time of retirement was Rs. 5,000 p.m. Compute the taxable amount from salary and pension for the previous year 1996-97 in following situations if salary and pension are due on 1st of every month:

A. He gets $^1/_3$ rd of his pension commuted from his employer (which is Panjab Govt.) and gets Rs. 60,000 as commuted value.

B. He gets $^1/_2$ of his pension commuted from his employer (a company) and gets Rs. 90,000 as commuted value. Company has given him gratuity also.

C. He commutes $^3/_4$th of his pension during January 1997 and gets Rs. 1,35,000 as commuted value. He does not get any gratuity from his employer which is a company.

[Hints. A. Salary Rs. 15,000 + Pension Rs. 9,000; B. Salary Rs. 15,000 + Pension Rs. 6750 + Taxable commuted value Rs. 30,000; C. Salary Rs. 15,000 + Pension Rs. 11,250 + Taxable commuted value Rs. 45,000].

5. Amount received as Leave Encashment on retirement. [Section 10(10AA)].

(*a*) *Central/State Govt. Employees*—any payment received as the cash equivalent of the leave salary in respect of the earned leave to his credit at the time of his retirement or on leaving the service shall be fully exempted.

(*b*) *Other employees*—any payment received as the cash equivalent of the leave salary to his credit at the time of superannuation or on leaving the service *shall be exempted upto least of the following amounts*:

(*a*) Actual amount received;

(*b*) Amount calculated at average salary for eight months (average salary means average of salary drawn by employee during 10 months immediately preceding his retirement); or

(*c*) *Notified Limit.* The monetary ceiling has been removed and Central Govt. has assumed the power to specify such limits in Official Gazette with effect from assessment year 1989-90 which are as follows:

For employees retiring between

(*i*)	After Jan. 1, 1988 to 31.3.95	79,920
(*ii*)	After 31.3.95 but upto 30.6.95	1,30,320
(*iii*)	After 30.6.95	1,35,360

(*d*) the cash equivalent of the leave salary to his credit at the time of retirement. This amount is to be calculated by taking leave for one month (30 days) for every one year of service less leave already availed of.

Salary. It shall mean basic salary + DA (if given under the terms of employment or if it enters into pay for retirement benefits + commission on turnover achieved by him.

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This exemption is admissible only at the time of retirement, super-annuation or resignation. Leave encashment will be fully taxable if received during service. In case leave encashment is given to legal heirs of deceased employee it will be fully exempted.

Excess of the amount received over least of the above shall be taxable.

Illustration 17. Mr. X retires on 1st July 1996 after 18 years of service and receives Rs. 75,000 as amount of leave encashment for 15 months. His employer allows 45 days leave for every one year of service. During service he has already encashed leave for 12 months. Calculate the taxable amount of leave encashment if his salary during 1.7.95 to 1.7.96 was Rs. 5,000 p.m.

Solution

Calculation of taxable amount of leave encashment of Mr. X.

Leave due as per section 10(10AA) @ one month leave for every one year of service	= 18 months
Less: leave already availed	= 12 months
Leave due at the time of retirement	6 months
Limits: (*i*) Notified Limit	Rs. 1,35,360
(*ii*) 8 month's average salary (8 × 5,000)	Rs. 40,000
(*iii*) Cash equivalent of leave due at the time of retirement (6 × 5,000)	Rs. 30,000
(*iv*) Actual Amount Received	Rs. 75,000

Least of above *i.e.*, Rs. 30,000 is exempted

Taxable Rs. 75,000 – Rs. 30,000 = Rs. 45,000.

Q. No. 12

Mr. Ghosh retires on 31.10.96 after 20 years service and received Rs. 48,000 as leave encashment for 12 months. His employer allows him 1½ month of leave for every one year of service. He has already encashed leave for 18 months. His salary for 1995-96 was Rs. 3000 and from 1.4.1996 it was raised to Rs. 4,000 p.m. Compute the taxable amount of leave encashment.

[Hints. Exempted leave encashment Rs. 7,400; Average Salary Rs. 3,700 Taxable amount Rs. 40,600].

***6. Any amount received as compensation on termination of employment* (Section 10B).**

Such compensation is tax-free upto the limits given below provided he gets compensation under the provisions of the Industrial Disputes Act:

(*i*) An amount calculated in accordance with the provisions of clause (b) of Section 25F of the Industrial Disputes Act;

(*ii*) *Notified Limit.* The monetary ceiling has been removed with effect from assessment year 1989-90. The limit shall be prescribed by the Central Govt. from time to time in Official Gazette. This limit will not be less than Rs. 50,000.

(*iii*) Actual compensation received, whichever is less.

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Under Industrial Disputes Act, a workman is allowed retrenchment Compensation equal to 15 days's average pay for each completed year of service or any part thereof in excess of six months.

The limits of sec 10 (10B) shall not apply in cases where the Compensation is paid under any scheme approved by Central Govt.

7. Any payment received by an employee of public sector company [Section 10(10C)].

With effect from 1.4.87, *i.e.*, assessment year 1988-89 any payment received by an employee of public sector undertaking [or of any other company (with effect from assessment year 1993-94)] at the time of his voluntary retirement shall be fully exempted if such amount is received in accordance with any scheme which has been approved by the Central Government.

Conditions for exemption u/s 10(10C)

(*i*) Service of 10 years or more, or must have completed 40 years of age;
(*ii*) It is not applicable on directors of a company;
(*iii*) The object should be overall reduction of staff;
(*iv*) Vacancy so caused is not to be filled up and no job is to be given to employee in any other concern of same management.

Limits. Least of following is exempted :

(*i*) 3 months salary × completed years of service,
(*ii*) Last salary drawn × balance months of service, before retirement,
(*iii*) Actual amount received; or
(*iv*) Notified limit Rs. 500,000.

Salary—has same meaning as for provident fund.

8. Any payment received from a Statutory Provident Fund or Public Provident Fund [Section 10(11)]. Fully exempted from tax.

9. Payment received from Recognised Provident Fund [Section 10(12)]. It is tax-free in following cases only:

(*a*) The employee has rendered 5 years' continuous service.
(*b*) Though he has not rendered 5 years' continuous service but the service has come to an end because of reasons beyond his control.

The Finance Act, 1974 has added a clarification to this exemption. If the accumulated balance standing in the name of employee is transferred from one recognised provident fund to another similar type of fund, such balance will not be added in the total income of the assessee. The period of five years will be counted by adding the period for which the fund remained with previous employer to the period for which the fund remains with the present employer from whom he is getting refund.

In case employee leaves service of his own accord before the expiry of 5 years, the amount on which tax has not been paid earlier is taxable under the head salary. As such taxable amount will be :

(*a*) Employer's contribution to RPF-upto 10% of employee's salary ; and
(*b*) Interest credited on RPF balance-upto 12% pa.

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10. Any payment from superannuation fund [Section 10(13)].

Any payment from an approved superannuation fund made—

(*i*) on the death of a beneficiary; or

(*ii*) on retirement or on becoming incapacitated; or

(*iii*) by way of refund of contribution on the death of a beneficiary; or

(*iv*) any refund of contributions of employee earlier than his retirement or on his becoming incapacitated to the extent of his own contribution made prior to the commencement of this Act and interest thereon, shall be fully tax-free.

11. House Rent Allowance [Section 10(13A)]. Explained earlier in allowances.

12. Any special allowance [Section 10(14)].

If any allowance is given by employer to employee to meet certain expenditure wholly and exclusively incurred in the performance of duties it is tax-free upto the extent it is incurred for such purposes such as out of pocket allowance or outfit allowance received by N.C.C. officers.

This section does not grant any exemption for any allowance given to meet the expenses at a place where the employee ordinarily resides and performs duties, *e.g.*, City Compensatory Allowance which is fully taxable.

DEDUCTIONS OUT OF GROSS SALARY [SECTION 16]

To calculate the taxable income under the head 'Salaries' following three deductions are allowed. Upto assessment year 1974-75 there were five deductions u/s 16. These deductions covered the expenditure on books, conveyance, professional tax and such other expenses but with effect from assessment year 1975-76 these deductions were replaced by only three deductions as given below:

1. **Standard Deduction** *(Expenditure incidental to employment)* [Section 16(1)]. This deduction is admissible to all salaried employees and pensioners also.

Rate of Standard Deduction

(a) For all employees [male or female] whose income under the head salary [before allowing standard deduction u/s 16(i)] does not exceed Rs. 60,000—33.33% of gross salary or Rs. 18,000 p.a. whichever is less.

(b) For all male employees or female employees whose total income exceeds Rs. 75,000

— $33^1/_3$% of Gross salary subject to a maximum of Rs. 15,000.

Standard deduction at the above rate shall be allowed even if employee has been given a car by the employer for his/her personal and family use.

For this purpose the term 'Salary' will include pension, fees, commission, perquisites or profits in lieu of salary, but will not include any payment received by the employee which is specifically exempt from tax under clauses (10), (10A), (10B), (11), (12) and (13A) of Section 10 of Income Tax Act. Simply, it means 'Gross Salary' computed according to the provisions given above.

The Finance Act (2) 1980 has amended the definition of the word 'salary' for the purpose of computation of standard deduction. Previously the standard deduction

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was allowed on any salary received *from employment* but with effect from 1.4.81 the words "from employment" have been deleted. Its effect is that the amount of pension received and if included in gross salary which was not eligible for standard deduction, shall be eligible for deduction.

The Finance Act, 1981 has further clarified that pensioners will also be entitled to claim this standard deduction.

Actual expenses incurred by the employee in connection with his earning of salary income are to be ignored.

(c) For female employees whose total income does not exceed Rs. 75,000

The Finance Act 1993 has increased the rate of standard deduction for women employees whose total income (before allowing deduction under this clause) does not exceed Rs. 75,000. ***It will be 33$^{1}/_{3}$% of gross salary or Rs. 18,000 p.a. whichever is less with effect from assessment year 1994-95.***

The higher rate of standard deduction for female employees will be allowed only if their total income i.e. income under all other heads such as house property, profits and gains, capital gains, income from other sources and gross salary and after allowing deductions u/s 80 does not exceed Rs. 75,000.

Example : Mrs. Santosh has gross salary of Rs. 60,000 and has income from other sources Rs. 14,000. Her total income is Rs. 74,000 hence she will get standard deduction of Rs. 18,000.

Suppose her other income from company dividend is Rs. 20,000. Her gross total income shall be Rs. 60,000 + Rs. 20,000 = Rs. 80,000 and she is entitled to a deduction u/s 80L for Rs. 10,000. Her total income shall be Rs. 70,000 and she is still eligible to get standard deduction of Rs. 18,000

But if her dividend income is Rs. 30,000, her total income after allowing deduction u/s 80L shall be Rs. 80,000 hence she will be eligible to get standard deduction up to Rs. 15,000 only.

> With effect from assessment year 1998-99 the rate of standard deduction has been made uniform for all employees and rate has been increased to 33.33% or Rs. 20,000 p.a. whichever is less. This deduction will be allowed on aggregate of gross salary received from both present and past employer in case employee has worked under more than one employer in one previous year.

2. **Entertainment Allowance** [Section 16(*ii*)]. See under allowances.

3. **Tax on Employment** [Section 16(*iii*)]. In case any sum is paid by the assessee on account of a tax on employment with the meaning of clause (2) of article 276 of the constitution leviable by or under any law, such amount shall be fully allowed as deduction. The example of this tax is professional tax levied by any State Government.

Illustration 18. Mr. Nath, an employee of Hindustan Lever since 1.4.54, is drawing a salary of Rs. 6,000 including D.A. of Rs. 1,000 p.m. From the very beginning he was getting entertainment allowance, and last year his E.A. was doubled. At present he is drawing Rs. 700 p.m. as Entertainment Allowance. The other perquisites are of Rs. 1,000 p.m.

Calculate his taxable salary.

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Solution. *Computation of salary income of Mr. Nath*

	Rs.
Salary @ Rs. 6,000 p.m. including D.A. of Rs. 1,000 p.m.	72,000
Perquisites @ Rs. 1,000 p.m.	12,000
Entertainment Allowance (E.A.) @ Rs. 700 p.m.	8,400
Gross Salary	92,400

Deductions:	Rs.	
Standard Deduction u/s 16(i) Restricted to Maximum:	15,000	
Entertainment allowance u/s 16(ii) (as calculated below)	4,200	
		19,200
Salary Income		73,200

Calculation of Entertainment Allowance deduction:

	Rs.
(*i*) Notified limit	7,500
(*ii*) 1/5 of Salary (Excluding D.A.)	12,000
(*iii*) E.A. drawn in 1954-55 @ 350 p.m. (being least)	4,200
(*iv*) E.A. drawn at present	8,400

So out of the four items, the third, *i.e.*, Rs. 4,200 being the least is allowed as deduction.

Illustration 19. Mr. Ajay is an employee drawing a salary of Rs. 1,000 p.m. He is provided with a rent-free unfurnished accommodation, the municipal value of which is Rs. 3,000 p.a. He is drawing entertainment allowance of Rs. 200 p.m. (in 1954-55, he was getting Rs. 150 p.m. as entertainment allowance). He is also enjoying the facility of a small car both for his official and personal use.

Calculate Mr. Ajay's taxable salary.

Solution. *Computation of Salary Income of Mr. Ajay*

	Rs.
Salary @ Rs. 1,000 p.m.	12,000
Entertainment allowance @ Rs. 200 p.m.	2,400
Car perquisite (As the salary of the assessee is less than Rs. 24,000, so car perquisite is not taxable)	NIL
Value of Rent-free Accommodation (As calculated below)	1,260
Gross Salary	15,660

Deductions:	Rs.	
Standard Deduction u/s 16(i) [33$^1/_3$%]	5,220	
Entertainment allowance u/s 16(ii) (As calculated below)	1,800	
		7,020
Salary Income		8,640

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Notes: (*i*) Value of Rent-free Accommodation:

Salary for this purpose [Salary Rs. 12,000 + Rs. 600 as taxable part of entertainment allowance] = 12,600	
Fair Rent: Municipal value of the house Rs. 3,000	
10% of Salary = (10% × 12,600)	1,260
Add: Excess of F.R.V. over 50% of Salary:	
(Fair Rent–50% of salary) (3,000–6,300)	NIL
Value of Rent-free Accommodation	1,260

(*ii*) *Entertainment Allowance:*

(1)	Rs. 7,500	
(2)	Actual E.A. drawn	2,400
(3)	1/5 of salary	2,400
(4)	E.A. drawn in 1954-55	1,800 (least)

The least of these items is allowed as deduction.

Illustration 20. From the following particulars, find out the taxable salary of Mrs. Asha.

(*a*) Salary Rs. 2,000 p.m.

(*b*) D.A. Rs. 1,500 p.m.

(*c*) Employer's contribution to Employee's Recognised Provident Fund—12% of basic salary.

(*d*) Rent-free accommodation (unfurnished)—fair rental value is Rs. 6,700 p.a.

(*e*) Interest on Provident Fund balance @ 13% p.a.—Rs. 3,900.

(*f*) A car (14 H.P.) is provided by employer. All expenses are borne by employer. It is used both for performance of duties and private purposes. Car was used by employee for only 11 months during the year.

(*g*) She paid professional tax of Rs. 200 and spent Rs. 300 on books and magazines.

Solution. *Computation of Salary Income of Mrs. Asha*

	Rs.	Rs.
Salary @ Rs. 2,000 p.m.		24,000
D.A. @ 1,500 p.m.		18,000
Employer's contribution towards RPF	2,880	
Less: exempted upto 10% of salary	2,400	
		480
Interest credited on R.P.F. Balance @ 13%	3,900	
Less: exempted (3,900 × 12/13) 12%	3,600	
		300

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Value of Rent-free Accommodation (unfurnished) (salary 24,000 F.R.V. 6,700)		
10% of salary	2,400	
Add: Excess of F.R.V. over 50% of salary (6,700 – 12,000)	NIL	
		2,400
Value of Car perquisite (14 H.P.) @ Rs. 600 p.m. × 11 months		6,600
Gross Salary		51,780
Less deductions:		
Standard Deduction u/s 16(i) [33$^1/_3$% of 51,780 or Rs. 18,000 whichever is less]	17,260	
Professional Tax u/s 16(iii) Full	200	
		17,460
Salary Income		34,320

Note: D.A. is not added in salary for the calculation of value of rent-free accommodation because it does not enter into service benefits.

Illustration 21. Shri Sham Lal's service was terminated by his employer on 31st Dec. 1996. He was drawing salary of Rs. 2,000 p.m. While in service he was a member of unrecognised provident fund, in which his employer was contributing the same amount as the employee was contributing. On his retrenchment, he got Rs. 12,000 from the unrecognised provident fund. On 1st March 1997 he got another job in a Bank at a salary of Rs. 2,800 p.m. His salary is due on last date of every month.

Solution

Computation of Mr. Sham Lal's Salary Income:	Rs.
Salary from April to Dec. 1996 @ 2,000 p.m. (9 months)	18,000
Salary for the month of March 1997 (New employer)	2,800
Amount received from Unrecognised Provident Fund excluding employee's own contribution and interest thereon (12,000 – 6,000)	6,000
	26,800
Gross Salary	
Standard Deduction 33$^1/_3$% of 26,800	8,933
	17,867
Salary Income	

Illustration 22. Shri Basu, an employee of a company, shows the following particulars of his income for the year ended 31st March 1997:

(*a*) Salary @ Rs. 4,000 p.m.

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(*b*) Following amounts have been paid by the employer company on behalf of employee in addition to salary:

(*i*) Rent-free unfurnished house—rent paid is Rs. 400 p.m.

(*ii*) Club Bills (Personal of Mr. Basu) Rs. 1,600 p.a.

(*iii*) Car allowance amounting to Rs. 6,000
Actual expenses are Rs. 5,000.

(*iv*) Insurance premium on assessee's life Rs. 900 p.m.

(*v*) Entertainment allowance amounting to Rs. 2,000 p.a. (regularly paid by employer company since 1953).

Find out his taxable salary. *[C.U., B.Com., (Hons.) adapted]*

Solution

Computation of Salary Income of Shri Bimal

Salary :	Rs.	Rs.	Rs.
Salary @ 4,000 p.m.		48,000	
Car Allowance Received	6,000		
Less: Actual expenses	5,000		
		1,000	
Entertainment allowance		2,000	
Perks:			
(*i*) Club Bill paid by employer u/s 17(2)(*iv*)		1,600	
(*ii*) Insurance Premium paid by employer u/s 17(2)(*v*)		10,800	
(*iii*) Rent-free house u/s 17(2)(*i*)			
F.R.V. Rs. 400 p.m. = Rs. 4,800 p.a.			
[Salary Rs. 48,000 + 1,000 = Rs. 49,000]			
10% of salary = Rs. 4,900			
As FRV is less than 10% of salary			
hence F.R.V. is taxable		4,800	
Gross Salary			68,200
Deductions u/s 16:			
u/s 16(i): Standard Deduction			
$33^1/_3$% of Rs. 68,200 or			
Rs. 15,000 whichever is less		15,000	
u/s 16(ii): Entertainment Allowance			
Least of following:			
(*a*) Statutory Limit	7,500		
(*b*) 1/5th of 48,000	9,600		
(*c*) E.A. received now	2,000		
(*d*) E.A. received (During 54-55)	2,000	2,000	
			17,000
Income under the head "Salaries"			51,200

Illustration 23. Mr. Srihari is appointed as a General Manager of Tubelight Company Ltd., Madras, on 1st February 1992 on the scale of Rs. 1,800—100—2,800. His annual increment of Rs. 100 falls due on 1st February of every year.

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Dearness allowance 100% of salary. Salary falls due on 1st day of every month. Bonus during the year Rs. 5,000, C.C.A., Rs. 400 p.m. Srihari's contribution to Recognised P.F. is at ***9% of basic pay and D.A.*** Equal contribution is made by his employer.

He is in possession of a company car for his official duties (for personal use also) with 14 H.P. All expenses including the driver's salary are met by the company.

A free accommodation has been provided. Rent paid by the company Rs. 1,800 p.m. Cost of Furnishing the home Rs. 48,000. He receives Rs. 500 p.m. as entertainment allowance. He was not receiving this allowance from his former employers before 1.4.1955. The company has reimbursed Rs. 12,000 being the actual Air Fare to and from Madras to attend the company's work.

He has insured his life for Rs. 50,000 and his wife's life for Rs. 20,000 for which the monthly premium is Rs. 250 and Rs. 300 respectively.

The City Improvement Trust Board has allotted him a site for which he has paid Rs. 9,600; being the part value during the year. Interest received on Fixed Deposit Rs. 340.

Compute his 'taxable' income under the head 'salaries' for the assessment year 1997-98.

Solution. *Computation of Salary Income of Mr. Srihari*

	Rs.	Rs.
Basic salary (See Note 1)		26,500
Dearness Allowance @ 100% of 26,500		26,500
Bonus		5,000
City Compensatory Allowance @ Rs. 400 p.m.		4,800
Employer's contribution to employee's RPF		NIL
Car Exp. met by employer: partly for personal		
Car of 14 H.P. @ Rs. 600 p.m.	7,200	
Driver @ Rs. 300 p.m.	3,600	10,800
Entertainment allowance @ Rs. 500 p.m.		6,000
Value of Rent-free accommodation in Madras		
Salary for this purpose = 26,500 + 5,000 + 4,800 + 26,500 + 6,000 = 68,800		
Fair Rental Value Rs. 21,600		
Cost of furniture Rs. 48,000		
10% of employee's salary	6,880	
Add: Excess of F.R.V. over 60% of salary [21,600 – 41,280]	NIL	
	6,880	
Add: 10% of cost of furniture	4,800	11,680
Gross Salary		91,280

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Deductions:		
Standard Deduction u/s 16(i)	15,000	
Entertainment Allowance u/s 16(ii)	NIL	
		15,000
Income under the Head "Salaries"		76,280

Note 1. *Salary fixation*

1.2.1992 to 31.1.1993	1,800 p.m.
1.2.1993 to 31.1.1994	1,900 p.m.
1.2.1994 to 31.1.1995	2,000 p.m.
1.2.1995 to 31.1.1996	2,100 p.m.
1.2.1996 to 31.1.1997	2,200 p.m.
1.2.1997 to 31.1.1998	2,300 p.m.

	Rs.
Salary for 11 months @ 2,200 p.m. (1.4.96 to 1.2.97)	24,200
Salary for 1 month @ 2,300 p.m. (due on 1.3.97)	2,300
Salary	26,500

REBATE OF TAX [Section 88]

To encourage savings, a rebate of tax for contributions towards provident funds (including superannuation funds), payment of life insurance premiums and depositing of money in the post-office under Cumulative Time Deposit (C.T.D.) scheme etc. are allowed from total tax.

Qualifying Amount [Q.A.] for Rebate of Tax

(*i*) ***Provident Fund***—Employee's own contribution to—
- (*a*) Statutory Provident Fund—Fully qualifies
- (*b*) Recognised Provident Fund—Fully qualifies
- (*c*) Public Provident Fund—Fully qualifies
- (*d*) Approved Superannuation Fund—Fully qualifies.

(*ii*) ***Life Insurance Premium.***

(*a*) On his own life; (*b*) On his wife's life; (*c*) On the life of all dependent children; and (*d*) On the joint life with any member mentioned above. Actual amount of premium paid by employer or employee shall fully qualify for rebate u/s 88.

Any amount received on maturity of life insurance policy and bonus thereon is fully exempted [Section 10(10D)]. This provision has been inserted by the Finance Act (2) 1991 with retrospective effect from 1.4.62.

(*iii*) Any amount contributed by an employee towards *group insurance scheme* of central or State Govt. fully qualifies for rebate u/s 88.

(*iv*) ***Unit Linked Insurance Plan of U.T.I. and L.I.C.***

Any amount paid by way of contribution towards Unit Linked Insurance Plan on own life or on the life of spouse shall qualify for rebate in the same manner as Life Insurance Premium. If a person withdraws from this scheme before the expiry

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of five years, the exemption already given shall be withdrawn. If withdrawal takes place after 5 years, full amount shall be tax-free.

(v) ***Cumulative Time Deposit (C.T.D.)***

The amount deposited in post office C.T.D. (10 years or 15 years) Account will fully qualify for deduction.

(vi) ***National Savings Certificates (VIII issue)***

Any amount deposited by assessee in post office to purchase National Savings Certificates (VIII issue) on his own name, on the name of his wife or on the name of any child shall fully qualify for rebate.

Any interest which accrues on VIII issue of National Savings Certificates shall also qualify automatically for this rebate in the year in which it accrues.

RATES OF INTEREST ACCRUED ON N.S.C. VIII ISSUE

At the end of	1 year	2 years	3 years	4 years	5 years	6 years
Purchased on or after 1.4.89	12.4%	13.9%	15.6%	17.6%	19.7%	22.4%

(vii) ***Any sum paid by an employee in an approved superannuation fund, during the previous year fully qualifies.***

(viii) ***Repayment of House Building Advance or Payment of instalment of price of House.***

As an incentive to build more residential houses, Govt. has allowed the following payments to be eligible for rebate u/s 88.

(*a*) any amount paid during relevant previous year towards self financing scheme of any development authority, housing board or other authority engaged in the construction and sale of any residential house property;

(*b*) any amount repaid for loans borrowed by the tax payee from the Government, any bank, life insurance corporation or such other institutions which are engaged in providing loans for construction of houses (*e.g.*, H.D.F.C., H.U.D.C.O., Housefed or National Housing Bank etc.) or to the employer if employer happens to be a public limited company; or

(*c*) any amount spent on stamp duty, registration fees and other expenses incurred for the purpose of transfer, shall qualify for rebate upto actual amount paid during the year or **Rs. 10,000** whichever is less.

Amount referred above should not include any interest which is allowable as deduction under the head income from House Property.

(ix) ***Amount paid in any scheme of National Housing Bank.***

Any subscription paid by an Individual or H.U.F. towards a deposit scheme of the National Housing Bank which the Central Govt. may specify in its Official Gazzette, shall also qualify for rebate of tax u/s 88 along with other savings.

(x) ***Any subscription to any deposit scheme of—***

(*a*) Public Sector Company engaged in providing long-term finance for construction or purchase of houses in India for residential purposes; or

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(*b*) any authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages or both. These schemes should be such that the interest on such deposits is not eligible for deduction u/s 80L and these must be notified by Central Government.

(*xi*) *Any amount invested by assessee in Jeevan Dhara or Jeevan Akshay policy of Life Insurance Corporation* shall fully qualify.

(*xii*) *Any amount invested in notified units of UTI or other mutual funds under Equity Linked Deposit Scheme* shall qualify *upto* actual amount invested or **Rs. 10,000** which ever is less.

(*xiii*) *Any amount invested in notified deposit scheme of Govt. i.e. National Saving Scheme 1992* shall fully qualify for this rebate.

(*xiv*) *Any amount deposited in pension funds set up by Mutual Funds (so notified) or U.T.I.* shall fully qualify.

(*xv*) Any amount subscribed under *Home Deposit Account* of a public sector company or an authority set up in India, which are engaged in providing long term finance for purchase or construction of houses for residential purposes or which is engaged in providing housing accomodation or improvement of cities and villages in India, shall fully qualify.

(*xvi*) *Amount paid as subscription to equity shares or debentures of any eligible issue*. In case such issue is notified by CBDT, the amount invested shall qualify for rebate u/s 88. The amount so invested and on which rebate is claimed shall not qualify for exemption of capital gain u/s 54EA or u/s 54EB.

(*xvii*) *Amount paid as subscription to any units of any mutual fund.* In case such unit scheme of mutual funds is notified by CBDT, the amount so invested shall qualify for rebate u/s 88. The amount so invested and on which rebate is claimed shall not qualify for exemption u/s 54EA or u/s 54EB.

The shares, debentures or units acquired under (xvi) and (xvii) above cannot be converted into money for three years. In case such units or shares are sold or otherwise transferred before the expiry of three years, the amount of rebate claimed shall become tax payable of the year in which these are sold or otherwise transferred.

Rate of Rebate of Tax

On qualifying amount as calculated above a rebate of tax out of total tax liability is allowed @ 20% of Qualifying Amount. In no case this rebate can exceed Rs. 12,000 for an ordinary individual whereas for special individuals like actors, singers, authors, Play writers, sports persons and artists this limit is Rs. 17,500 in a previous year and rate is 25% of qualify amount provided 25% of total income is from such profession.

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In case any individual has made investment under point (xvi) or (xvii) above the maximum amount of rebate shall not exceed Rs. 14,000.

Illustration 24. Mr. Mohan's total income is Rs. 1,00,000. He contributes Rs. 500 p.m. towards Recognised Provident Fund. He is insured for Rs. 1,80,000 and is paying a premium of Rs. 20,000 annually. He is also depositing Rs. 250 p.m. in 10 year Cumulative Time Deposit Scheme. He purchased N.S.C. VIII issue for Rs. 20,000 during the year.

Calculate the amount of rebate of tax u/s 88.

Solution

The qualifying amount will be the aggregate of the following items. The items are:

		Rs.
(*i*)	Life insurance premium	20,000
(*ii*)	Provident Fund Contribution—Actual Contribution	6,000
(*iii*)	10 year C.T.D. @ Rs. 250 p.m.	3,000
(*iv*)	N.S.C. purchased VIII issue	20,000
	Total Contribution	49,000

Out of tax liability on income of Rs. 1,00,000 (*i.e.*, Rs. 15,000) Mr. Mohan can claim rebate of tax @ 20% of qualifying savings of Rs. 49,000 (*i.e.*, Rs. 9,800). Maximum rebate allowed under this section is Rs. 12,000. Tax liability in this case shall be Rs. 15,000 – Rs. 9,800 = Rs. 5,200.

Q. No. 13

(*a*) From the following information calculate tax rebate allowable U/s 88 to Sri Verma for the Assessment Year 1997-98

(1) LIC Premium of Rs. 6,000 paid on his own life policy of Rs. 50,000.

(2) National Savings Certificate VIII Issue purchased Rs. 10,000.

(3) Rs. 5,000 subscribed for the Home Loan account of the National Housing Bank.

(4) Rs. 8,000 paid to the Mutual fund of M.E.P of U.T.I.

(5) Rs. 4,000 contributed to Unit Linked Insurance Plan of U.T.I.

(6) Rs. 2,000 contributed to unrecognised provident fund.

(7) Rs. 7,000 accrued interest on NSC VIII issue.

(8) Repayment of Rs. 12,000 towards the Housing loan.

(9) Rs. 1,000 contributed to Post Office Savings Bank account.

(*b*) What will be the amount of rebate u/s 88 if Sri Verma is anauthor and his total income includes 25% from royalty ? (*B.Com. Manglore, April-1994*)

[Hints. (*a*) Q.A. Rs. 50,000; Rebate u/s 88 @ 20% Rs. 10,000

(*b*) Rs. 12, 500.]

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CHART SHOWING COMPUTATION OF INCOME FROM SALARIES

Item	*Treatment*
I. Salary	
(*i*) **Pay/Salary/Wages/ Basic Pay**	Fully Taxable u/s 15 (Whether received from present or past employer)
(*ii*) **Bonus**	Fully Taxable u/s 15
(*iii*) **Commission**	Fully Taxable u/s 15 (will be treated as salary if given as fixed (%) percentage of sale achieved by him)
(*iv*) **Annuity**	Fully Taxable u/s 15
(*v*) **Pension**	Fully Taxable u/s 15
(*vi*) **Salary in lieu of leave**	Fully Taxable u/s 15
(*vii*) **Annual Accretion to R.P.F.**	(*i*) Excess of employer's contribution to recognized provident fund over 10% of employee's salary—to be added in salary. [Salary = Pay + D.P./D.A. (D.A. if it enters into pay)]. (*ii*) Excess of interest credited to employee's accumulated balance of R.P.F. over prescribed rate.
(*viii*) **Transferred Balance**	Balance transferred from unrecognised provident fund to recognized provident fund is called Transferred Balance. It is to be treated as R.P.F. from the day it was instituted and exemption is to be allowed as in annual accretion.
(*ix*) **Any advance Salary**	Fully Taxable.
II. Allowances	
1. **Dearness Allowance (D.A.)/Dearness Pay (D.P.)/Additional Dearness Allowance Interim Relief**	Fully Taxable
2. **House Rent Allowance (H.R.A.)**	U/s 10(13A) exempted upto least of the following: (*a*) Actual allowance received: (*b*) Actual rent paid *less* 1/10th of salary: (*c*) 50% of salary in case of Bombay, Calcutta, Delhi & Madras and 40% of salary in case of all other cities. Excess of H.R.A. received over exempted limit is taxable. [*Note:* Salary = Basic Salary + D.A./(If provided under the terms of employment or D.P. (In case of Govt. employees) + Commission given as fixed (%) percentage of sale achieved by employee] If employee is living in a house for which he is not paying any rent, full HRA is taxable.

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Item	*Treatment*
3. **City Compensatory Allowance (C.C.A.)**	Fully taxable
4. **Conveyance Allowance (C.A.)**	U/s 10(14) exempted upto the actual expenditure incurred wholly and necessarily for the purposes of employment. Excess of C.A. received over actual expenditure is taxable.
5. **Travelling Allowance (T.A.)**	Exempted as per notification issued u/s 10(14).
6. **Entertainment Allowance (E.A.)**	Fully added in salary. But Govt. employees are entitled to a deduction u/s 16(*ii*)(*a*) at the rate of least of the following: (*i*) Rs. 5,000 p.a; (*ii*) 1/5th of salary (only basic); or (*iii*) Actual E.A. received and in case of other employees u/s 16(*ii*)(*a*) at the rate of least of the following: (*i*) Rs. 7,500 p.a.; (*ii*) 1/5th of salary (only basic); (*iii*) Actual E.A. being received; or (*iv*) Amount of E.A. received before 1.4.55. Conditions for *other employees* to claim this deduction: (*i*) Employee is working under the same employer since before 1.4.55. (*ii*) and he was getting this allowance before 1.4.55.
7. **Allowance given to employee's of the transport system**	Exempted upto 70% of such allowance or Rs. 3,000 p.m. whichever is less provided no daily allowance is received in respect of such duties.
8. **Allowance for helper**	Fully exempted if given for employment of helper for official duties.
9. **Education Allowance (Ed.A.) or Reimbursement of Tuition Fee**	Exempted upto Rs. 50 p.m. per child for two children only. and Rs. 150 p.m. if child is in Hostel.
10. **Foreign Allowance**	Fully exempted if paid to Govt. employees working outside India. u/s10(7)
11. **Uniform Allowance or outfit Allowance**	Fully exempted u/s 10(14).
12. **Any other Allowance u/s/ 14**	Exempted as per notification issued under section 10(14)
III. Perquisites (Perks)—Taxable in all Cases	
1. **Rent Free House**	**(In case of employees other than Government or semi-Government or Reserve Bank of India) Value of such benefit taxable u/s 17(2(*i*)—**

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Item	*Treatment*
	Valuation: Requirements: (*i*) Fair Rental Value (F.R.V.) it will include any salary paid by employer to gardener if house is owned by employer. (*ii*) Whether furnished or unfurnished. (*iii*) Salary [Pay + D.A. (if added for service benefits + Bonus + Commission + Taxable Portion of E.A., C.A., and Ed.A. and other taxable allowances) + Income-tax and Professional tax paid by or reimbursed by employer]. (*iv*) If furnished, cost of furnishing or actual hire charges of furniture. (*v*) Place of employment—Delhi, Bombay, Calcutta, Madras or any other Town. *Method: Unfurnished:* (*i*) If F.R.V. is less than 10% of salary the value of perquisite will be F.R.V. (*ii*) If F.R.V. is more than 10% of salary: (*a*) F.R.V. upto first 10% of salary = Taxable. (*b*) Excess of F.R.V. over 50% of salary = Taxable. Add (*a*) and (*b*) to get value of perquisite. In Bombay, Calcutta, Madras and Delhi—the method will be (*a*) F.R.V. upto first 10% of salary = Taxable. (*b*) Excess of F.R.V. over 60% of salary = Taxable. Add (*a*) and (*b*) to get value of perquisite. *Furnished:* (*i*) *Calculate* the value of unfurnished house as per above. (*ii*) Add 10% of cost of furnishing or hire charges of furniture in this value. The total will be value of furnished house.
2. Concessional Rent Accommodation	Taxable u/s 17(2)(*ii*) for every employee. In this case employee gets a house from employer but pays concessional rent. The value of perquisite shall be as below: (*i*) Calculate the value of furnished or unfurnished house as per above. (*ii*) Deduct the amount of rent paid by employee. The balance, if any, will be the value of perquisite.
Taxable in specified cases only	Taxable u/s 17(2)(*iii*)—for only those employees, who are either (*a*) directors of companies; or (*b*) have substantial interest in the affairs of company, *i.e.*, they hold more than 20% of voting rights or (*c*) their monetary salary after allowing deductions u/s 16 exceeds Rs. 24,000 p.a.
(*i*) Motor Car	If car is provided by employer for (*a*) only official use—the value of perquisite will be nil.

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Item	*Treatment*
If Salary exceeds 24000 then C.A is provided. and is taxable.	(*b*) only personal use—the value of perquisite will be the total expenditure incurred by employer on the running and maintenance of such motor car plus normal wear and tear of the car. (*c*) partly for official and partly for personal purposes—the value will be as under: *Not exceeding* 16 H.P. / *Exceeding* 16 H.P. (*i*) Expenses for private use met by employer Rs. 600/- p.m. / Rs. 800/- p.m. (*ii*) Expenses met by employee Rs. 200/- p.m. / Rs. 300/- p.m. If chauffeur is also provided add Rs. 300/- p.m. in the above values.
(*ii*) **Any other conveyance**	Assessing Officer to decide the value of perquisite.
(*iii*) **Free transport or carriage facilities provided by employer**	Not Taxable u/s 17(2)(iii) for self, family and dependents, if employer is running transportation business.
(*iv*) **Free Domestic servants**	Taxable u/s 17(2)(*iii*) at the rate of Rs. 120/- per month per person. [watchman, sweeper, gardener]
(*v*) **Free gas, electric energy or water supply**	Taxable u/s 17(2)(iii) as per below: (*a*) *Actual amount* of bill paid to a supplying agency. (*b*) Nil—if supplied from employer's own resources. (*c*) When consumed for official duties also proportionate actual expenditure upto a maximum of 6-1/4% of salary.
(*vi*) **Free Boarding and Lodging**	Taxable u/s 17(2) as per below: *Hotel employees:* (*a*) Boarding—Actual cost of food and facilities supplied. (*b*) Lodging—same rules as for other employees. *Other employees:* Actual bill met by employer.
(*vii*) **Free Education Facilities**	Actual expenditure incurred by employer or the cost which employee, would have incurred in similar institution in or near locality, shall be the value of perquisite taxable u/s 17(2)(*iii*).
(*viii*) **Free Medical Facilities**	Exempted
(*ix*) **Recreational Facilities**	Exempted
(*x*) **Refreshment provided during working hours to all employees**	Exempted

as per executive instructions (For detail please see text)

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Item	*Treatment*
(*xi*) **Free Lunch/Dinner**	Exempted if given to all employees during working hours but value is taxable on actual basis only for specified employees in case it is provided to one of the employees.
3. **Obligation of employee met by employer**	Taxable in case of every employee u/s 17(2)(*iv*). (*i*) Club Bills and subscriptions. (*ii*) Tiffin or lunch allowance. (*iii*) Tax liability of employee. (*iv*) Salary of gardener or servant, if it is given as allowance to employee.
4. **Life Assurance Premium/Annuity**	Taxable as perquisite if paid by employer u/s 17(2)(*v*).
IV. Profits in Lieu of Salary	
1. **Retrenchment Compensation**	Fully taxable as salary u/s 17(3)—but subject to exemption u/s 10(10B) (only for workmen receiving compensation under Industrial Disputes Act (1947).
2. **Gratuity**	(*i*) U/s 10(10) Retirement gratuity is fully exempted in case of all government employees. (*ii*) In case of employees covered under Payment of Gratuity Act 1972—Exempted upto least of following: (*a*) Notified Limit Rs. 100,000. (*b*) 15 days average wages for every one completed year of service and fraction for 6 months or more to be counted as one year; (*c*) Actual amount received. (*iii*) In case of other employees, gratuity received is exempted upto least of the following and excess over exempted limit is taxable: (*a*) Actual gratuity received: (*b*) Notified Limit Rs. 2,50,000. (*c*) 1/2 month's average salary for every one year of service (Average salary means average of the salary drawn during 10 months before the calendar month of retirement).
3. **Commutation of Pension**	U/s 10(10A)—Any amount received by a Government employee as commutation of pension is fully exempted. But in case of any other employee it is tax-free upto the following limits: (*a*) ***If the employee gets gratuity:*** **Exempted upto commuted value of 1/3 of pension.**

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Item	*Treatment*
	(*b*) *If the employee does not get gratuity:* Exempted upto commuted value of 1/2 of pension.
4. **Leave Encashment**	(*A*) Govt. and Semi-Govt. employees— Fully exempted if received at the time of retirement.
	(*B*) In case of other employees exempted only at the time of retirement at the rate of least of following:
	(*a*) Actual amount received.
	(*b*) Eight month's average salary.
	(*c*) Notified Limit.
	(*d*) Cash equivalent of leave due at the time of retirement. *Excess taxable.*
5. **Refund of balance from Provident Fund**	(*i*) *From Statutory Provident Fund*— Fully Exempted.
	(*ii*) *From Recognised Provident Fund*—Fully exempted unless the employee leaves service of his own accord before the expiry of 5 year's continuous service. In this case taxable portion is to be added in salary.
	(*iii*) *From Un-Recognised Provident Fund*— Taxable portion to be added in salary. Taxable portion = Employer's contribution + Interest on this amount.
6. **Any other payment (Not in the nature of Personal gift)**	Fully Taxable.

DEDUCTIONS

1. **Standard Deduction u/s 16(l)**	Out of Gross Salary, assessee is entitled to claim this deduction irrespective of the fact whether he has spent any expenditure or not. *Rate of deduction:* $33\frac{1}{3}\%$ of gross salary, subject to a maximum of Rs. 15,000 (For females employee whose total income before allowing this deduction does not exceed Rs. 75,000 limit is Rs. 18,000) and for male employees whose income under the head salary before allowing this deduction does not exceed Rs. 60,000 the limit is Rs. 18,000.
2. **Entertainment Allowance u/s 16(*ii*)**	Deduction at the rates as given earlier in the text.
3. **Tax on Employment 16(*iii*)**	Full amount paid is allowed as deduction.

Rebate of Tax u/s 88

This rebate is allowed only out of tax liability and not out of salary income or out of Gross Total Income.

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Item	*Treatment*
1. **Qualifying amount for rebate in case of an Individual**	(*i*) Employee's own contribution to provident fund (*a*) To S.P.F. = Full (*b*) To R.P.F. = Full (*c*) To P.P.F. = Full (*d*) any amount paid by employee towards approved superannuation fund—Fully qualifies. (*ii*) Life Insurance Premium paid by employee or by employer: (*a*) On own life, (*b*) On the life of wife, (*c*) On the life of children, (*d*) On joint life with any member of family—Actual premium fully qualifies. (*iii*) Any amount contributed by employee towards group insurance scheme of State or Central Govt. (*iv*) Contribution to Unit Linked Insurance Plan = full amount. (*v*) Assessee's contribution to Post Office C.T.D. (10 years or 15 years A/c = Full). (*vi*) An amount deposited in Post Office to purchase National Saving Certificates VIII issue. (*vii*) any instalment or repayment of House Building Advance or payment of price of house purchased from Govt., or Housing Board or L.I.C. or National Housing Bank etc. Actual or Rs. 10,000 whichever is less. (*viii*) any amount paid in a deposit scheme of National Housing Bank. (*ix*) any amount invested in eligible shares, debentures, units of UTI or Mutual Funds (so notified) (*x*) Accrued interest on NSC (VIII issue).
2. **Rate of Rebate of tax**	Rebate of tax @ 20% of total savings but not exceeding Rs. 12,000 in a previous year. In case any amount is invested in point (ix) above, limit shall be raised to Rs. 14,000 p.a. For special individuals limit is 25% of savings or Rs. 17,500 w.e. is less.

Illustration 25. Mr. Z is an employee posted at Chandigarh. The following are the particulars of his salary income.

(*i*) Salary @ Rs. 2,000 p.m.

(*ii*) D.A. @ Rs. 250 p.m. (It enters into service benefits).

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(*iii*) Bonus Rs. 4,000.

(*iv*) He is provided with a rent-free unfurnished accommodation, the employer pays Rs. 500 p.m. for that accommodation.

(*v*) The employee contributes 12% of his salary towards his provident fund. The employer is also contributing the same amount.

(*vi*) He paid Rs. 5,000 as life insurance premium on his life. Compute his total income if the provident fund is:

(*a*) Statutory Provident Fund.

(*b*) Recognised Provident Fund.

(*c*) Unrecognised Provident Fund.

Solution

Computation of total income of Mr. Z:

Particulars		Under S.P.F.	Under R.P.F.	Under U.R.P.F.
Salary @ Rs. 2,000 p.m.		24,000	24,000	24,000
D.A. (Enters into pay) Rs. 250 p.m.		3,000	3,000	3,000
Salary		27,000	27,000	27,000
Bonus		4,000	4,000	4,000
Value of unfurnished house (See Note—1)		3,100	3,100	3,100
Employer's contribution to R.P.F. @ 12% of Rs. 27,000	= 3,240			
Less: 10% of salary	= 2,700			
Taxable for R.P.F. only	540	—	540	—
Gross Salary		34,100	34,640	34,100
Deduction u/s 16(i)				
Standard Deduction (33⅓%)		11,367	11,547	11,367
Salary Income being Total Income		22,733	23,093	22,733
Total Income (Rounded off)		22,730	23,090	22,730

Note 1. Calculation of value of rent-free house

at Chandigarh F.R.V. = Rs. 6,000 p.a.	
(Salary 24,000 + 4,000 + 3,000 = 31,000)	
10% of salary	= 3,100
Plus F.R.V. – 50% of salary (6,000 – 15,500)	Nil
Value	3,100

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Note 2. Calculation of Q.A. for rebate of tax u/s 88

	Rs.	Rs.	Rs.
Qualifying amount			
(*a*) Own contribution to P.F. (12% of salary)	3,240	3,240	Nil
(*b*) Life Insurance Premium	5,000	5,000	5,000
Q.A.	8,240	8,240	5,000

Illustration 26. The following are the particulars of salary income of Mr. Gama, who is employed at Kanpur:

(*a*) Salary @ Rs. 2,000 p.m.

(*b*) D.A. @ 40% of salary.

(*c*) Compensation received for termination of employment from previous employer Rs. 6,000.

(*d*) City Compensatory Allowance @ Rs. 200 p.m.

(*e*) House Rent Allowance Rs. 400 p.m. and he pays rent of Rs. 500 p.m.

(*f*) He is contributing Rs. 250 p.m. towards Recognised Provident Fund (R.P.F.). The employer is also contributing the same amount.

(*g*) During the year he paid Rs. 200 as professional tax.

(*h*) He owns a car which he is using for official and personal use.

Calculate his taxable income and Q.A. for rebate of tax u/s 88.

(B.Com., P.U.)

Solution. *Computation of total income of Mr. Gama*

	Rs.	Rs.
Salary @ Rs. 2,000 p.m.		24,000
D.A. @ 40% of salary		9,600
Employer's contribution to R.P.F. over 10% of employee's salary (3,000 – 2,400)		600
Compensation from previous employer [Profit in lieu of salary exempted u/s 10(10B)].		Nil
C.C.A. @ Rs. 200 p.m.		2,400
House Rent Allowance (H.R.A.)		
(*i*) H.R.A. drawn @ Rs. 400 p.m.	4,800	
(*ii*) 40% of salary (Kanpur)	9,600	
(*iii*) Excess of Rent paid over 10% of salary (6,000 – 2,400)	3,600 (least)	
So Rs. 3,600 is exempted out of Rs. 4,800 and the balance is added in salary		1,200
Gross Salary		37,800

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Less Deductions		
Standard Deduction u/s 16(*i*):		
$33^1/_3$% of Rs. 37,800	12,600	
Professional tax u/s 16(*ii*) Full	200	
		12,800
Salary Income		25,000
Add: Income from other heads		Nil
G.T.I. being Total Income		25,000

Rebate u/s 88: Qualifying amount:

Employee's contribution towards R.P.F. Rs. 3,000

Note: Compensation on retrenchment is not taxable as employee is covered under Industrial Disputes Act, 1948.

Illustration 27. Smt. Tej Kaur has furnished the following details with regard to her salary income:

(*a*) Salary of Rs. 3,000 per month.

(*b*) Bonus equal to six month's salary.

(*c*) Conveyance allowance at Rs. 300 per month.

(*d*) Entertainment allowance at Rs. 250 per month.

(*e*) Commission equal to four month's pay.

She is also provided with free furnished quarter valued at Rs. 400 per month for rent and Rs. 100 per month for furniture and fittings. She is also provided with free lunch by the company valued at Rs. 2 per day for 300 days. She is employed in this company since April 1959. She claims:

(*a*) Car maintenance expenses and depreciation on car at Rs. 500 per month (used for employment purposes).

(*b*) Cost of books and periodicals necessary for this work Rs. 1,200 in the year.

Her contribution to company's Recognised Provident Fund is Rs. 500 per month and employer contributes an equal sum.

The interest credited to the Provident Fund Account is Rs. 2,000 @ 10%. Compute her salary income. *(B.Com., P.U.)*

Solution. *Computation of salary income of Smt. Tej Kaur*

	Rs.
Salary @ 3,000 p.m.	36,000
Bonus equal to 6 months' salary	18,000
Entertainment allowance @ Rs. 250 p.m.	3,000
Commission equal to 4 months' salary	12,000
Value of rent-free furnished accommodation	
Fair Rent = Rs. 400 p.m. 4,800 p.a.	
[Salary = 36,000 + 12,000 + 18,000 + 3,000 = 69,000]	

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As F.R.V. is less than 10% of salary hence F.R.V. is taxable	4,800	
Add: Actual hire charges of Furniture	1,200	
		6,000
Lunch Rs. 2 per day for 300 days		600
Employer's Contribution towards employee's recognised provident fund over and above 10% of employee's salary (6,000 – 3,600)		2,400
Gross Salary		78,000
Standard Deduction u/s 16(i) (Maximum of Rs. 15,000 as her gross salary is more than Rs. 75,000)		15,000
Salary Income		63,000

Rebate u/s 88: Qualifying amount:

Contribution towards R.P.F. Rs. 6,000

Notes: 1. No deduction of Entertainment Allowance is allowed as the assessee was not getting any Entertainment Allowance before 1st April 1955.

2. Conveyance allowance is fully exempted.

Illustration 28. From the following particulars of Shri Yadunandan Upadhyay, compute his total income appending notes where necessary:

		Rs.
(*i*)	Salary Rs. 3,000 p.m.	36,000
(*ii*)	Bonus	6,000
(*iii*)	Dearness Allowance	1,800
(*iv*)	Entertainment Allowance (never given before)	5,000
(*v*)	Employer's contribution to Recognised P.F.	4,000
(*vi*)	Employee's contribution to Recognised P.F.	4,000
(*vii*)	Interest on P.F. @ 9%	2,000
(*viii*)	Personal expenses of Mr. Upadhayay's son met by the employer	1,000
(*ix*)	Rent-free unfurnished house provided by the employer, whose rental value is (city is Delhi)	6,000
(*x*)	Watchman engaged by the employer for many years for the security of residence of Shri Upadhyay, total salary paid to him by employer during the year	4,800
(*xi*)	Medical expenses of the employee and free refreshment during office hours	600
(*xii*)	Club bill of the assessee paid by the employer	400
(*xiii*)	Unit Linked Insurance Plan Contribution paid by the employer	1,000

(B.Com., P.U.)

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Solution. *Computation of Total income of Yadunandan*

		Rs.
Salary @ Rs. 3,000 p.m.		36,000
Bonus		6,000
Dearness Allowance		1,800
Entertainment Allowance (never given before)		5,000
Employer's contribution to employee's R.P.F. over 10% of employee's salary (4,000 – 3,600)		400
Perquisites		
Personal expenses met by the employer [17(2)(iv)]		1,000
Club bills paid by the employer [17(2)(iv)]		400
Unit Linked Insurance Plan Contribution paid by employer [17(2)(iv)]		1,000
Value of Rent Free Unfurnished Accommodation [17(2(i)]		
F.R.V. of the House Rs. 6,000 p.a.		
Salary = [36,000 + 6,000 + 5,000 = 47,000]		
10% of salary	4,700	
Add: Excess of F.R.V. over 60% of salary	Nil	
		4,700
Watchman: Rs. 120 p.m.		1,440
Gross Salary		57,740
Standard deduction u/s 16(i):		
$33^1/_3$% of 57, 740 *i.e.* Rs. 19,247 or Rs. 18,000 whichever is less as gross salary does not exceed Rs. 60,000		18,000
Salary income being Total Income		39,740

Rebate u/s 88: Qualifying Amount	Rs.
Contribution to R.P.F.	4,000
Unit Linked Insurance Plan Contribution	1,000
Qualifying Amount (Q.A.)	5,000

Notes: 1. Medical expenses and free refreshment during office hours are exempted perquisites.

2. No deduction is allowed regarding entertainment allowance as the assessee was not getting this allowance before 1st April 1955.

3. D.A. will not be added in salary for calculating the value of rent-free accommodation as D.A. does not enter into salary for calculating service benefits.

Illustration 29. Following particulars are furnished by Mr. P. a citizen and resident of India:

	Rs.
(*i*) Net salaries received after deduction of tax at source and of contribution to the Recognized P.F.	24,000
(*ii*) Tax deducted at source from salaries	7,000

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(*iii*)	Own contribution to R.P.F.		4,000
(*iv*)	Employer's contribution to R.P.F.		4,000
(*v*)	Interest credited to R.P.F. at the rate of 9% p.a.		4,000
(*vi*)	Travelling expenses for self and wife proceeding on leave to his home town		2,400
(*vii*)	House rent allowance (the house is in Calcutta and rent actually paid amounts to Rs. 5,400)		4,800
(*viii*)	Life Insurance Premia as follows: Premia paid:		
	(*a*) On own life—sum assured	Rs. 80,000	10,000
	(*b*) On wife's life—sum insured	Rs. 30,000	2,000
	(*c*) On minor son's life—sum assured	Rs. 10,000	800

Compute the Total taxable income of Mr. P.

(B.Com., P.U.)

Solution

Computation of Total Income of Mr. P.	Rs.	Rs.
Salary		
Net salary after deduction of tax at source and P.F. Contribution	24,000	
Add: Tax deducted at source	7,000	
Add: R.P.F. Contribution	4,000	
		35,000
Employer's Contribution towards R.P.F. in excess of 10% of employee's salary (4000 – 3,500)		500
House Rent Allowance (H.R.A.)		
(*i*) 50% of salary (Calcutta)	17,500	
(*ii*) Actual H.R.A. drawn	4,800	
(*iii*) Excess of Actual Rent paid over 10% of salary = (5,400 – 3,500)	1,900	
Taxable portion of H.R.A. Actual—Exempted (4,800 – 1,900)		2,900
Travelling Expenses for self and wife proceeding on leave to his home town [Exempted u/s 10(5)]		Nil
Gross Salary		38,400
Standard deduction u/s 16(i) 33$^1/_3$% of salary *i.e.* Rs. 12,800 or Rs. 18,000 w.e. is less		12,800
Salary Income being Total Income		25,600

Rebate u/s 88: Qualifying Amount	Rs.
Contribution to R.P.F.	4,000
Life Insurance Premia	
Self	10,000
Wife's life	2,000
Minor son's life	800
Q.A.	16,800

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Illustration 30. Mr. X is employed in a factory as an accountant on monthly salary of Rs. 2,800 plus a dearness allowance of Rs. 800 per mensem. He was provided with a scooter by his employer for the performance of his duties. He is a member of an unrecognised fund to which he contributes 10% of his salary and his employer also contributes an equal amount. On 1st August 1996 he resigned and joined another factory on the same date on a monthly salary of Rs. 3,000 plus a dearness allowance @ 10% of his salary. He received Rs. 10,000 from the unrecognised provident fund of which half of the amount consisted of employer's contribution and interest thereon. In his new employment he contributed 10% of his salary to a recognised provident fund while his employer contributed Rs. 3,040. He is also provided with an unfurnished rent-free house by the second employer, the municipal valuation of which is Rs. 1,500 per mensem. The second employer also allows free use of Maruti car to him. He pays Rs. 800 per annum as premium on his life insurance policy of Rs. 7,000 and deposits Rs. 1,000 in a 15 year Post Office Savings Bank Cumulative Time Deposit Account. Find out his total income, if salary falls due on 1st day of next month. *(B. Com., Kanpur)*

Solution

Computation of Total Income of Mr. X		Rs.
Salary:		
Pay @ Rs. 2,800 p.m. for 5 months		14,000
D.A. @ Rs. 800 p.m. for 5 months		4,000
Pay @ Rs. 3,000 p.m. for 7 months (second employer)		21,000
D.A. @ Rs. 300 p.m. for 7 months		2,100
Refund of balance from Unrecognised Provident Fund: Employer's contribution and interest thereon: 1/2 of Rs. 10,000		5,000
Excess of employer's contribution to R.P.F. Over 10% of employee's salary (3,040 – 2100)		940
Value of Rent-free Unfurnished Accommodation		
Rental value for 7 months @ Rs. 1,500 p.m.	10,500	
10% of salary (21,000 × 10%)	2,100	
Add: Excess of Rental value over 50% of salary	Nil	2,100
Value of small car : Exp. met by employer (600 × 7)		4,200
		53,340
Gross Salary		17,780
Standard Deduction u/s 16(i)		
$33^1/_3$% of 53,340 = 17,780		
as his gross salary does not exceed Rs. 60,000		35,560
Salary Income being Total Income		

Rebate of tax u/s 88: Q. A. for rebate	
1. Contribution to recognised provident fund	2,100
2. Life Insurance Premium:	800
3. Contribution to C.T.D.	1,000
	3,900
Q.A.	

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Illustration. 31

(*a*) Mr. X is working with Life Insurance Corporation of India at Delhi. His salary is Rs. 2,000 p.m. He gets D.A. @ 900 p.m. and 2/3 of which enters into pay for service benefits. The employer has provided him with a car of 800 c.c. (8 h.p.) with driver. The expenses are met by employer and is partly used for employment and partly for personal purposes. He is provided with a rent free house whose fair rental value is Rs. 24,000 p.a. Rent of furniture is Rs. 3,000 p.a.

Compute his salary income for the assessment year 1997-98.

(*b*) What difference it would make if he gets D.A. @ Rs. 1,200 p.m. and 1/2 of which enters into pay for service benefits ?

Solution. *Computation of salary income of Mr. X*

Particulars		(*a*) Rs.	(*b*) Rs.
Salary @ 2,000 p.m.		24,000	24,000
D.A. (*a*) 900 pm. ($^2/_3$ enters) (900 × $^2/_3$ × 12)		7,200	
		31,200	
Rest of D.A.	(300 × 12)	3,600	
(*b*) 1,200 p.m. ($^1/_2$ enters)	(600 × 12)		7,200
			31,200
Rest of D.A.	(600 × 12)		7,200
Car Perk : Small car—expenses met by employer; partly for personal with driver			
(*a*) Not taxable as employee is not covered under specified cases because salary does not exceed Rs. 24,000 [31,200 + 3600 = 34,800 less 1/3 standard Deduction 11,600 = 23,200] and he is neither a director nor holds 20% or more shares		NIL	
(*b*) Taxable @ Rs. 600 p.m. × 12 = 7,200			
Driver's salary Rs. 300 p.m. × 12 = 3,600			
			10,800
Value of rent free house			
F.R.V. Rs. 24,000 p.a.			
Rent of Furniture = Rs. 3,000 p.a.			
Salary = Rs. 31,200 Semi Govt. employee			
10% of salary = 3,120 or F.R.V. Rs. 24,000 whichever is less is taxable	= 3,120		
Add : Rent of furniture	3,000	6,120	6,120
Gross salary		40,920	55,320

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Standard Deduction u/s 16(*i*) 33$^1/_3$% or Rs. 18,000 whichever less as his salary does not exceed Rs. 60,000	13,640	18,000
Salary Income	27,280	37,320

Illustration 32. Mr. A.K. Gupta, who is neither a director nor has substantial interest in any company, is offered on April 1, 1996 an employment by XYZ Ltd., Chandigarh with the following two alternatives:

	Alternative I	*Alternative II*
	Rs.	Rs.
Basic pay	20,000	20,000
Bonus	2,000	2,000
Education allowance for the children	3,200	—
Education facility	—	3,200
Servant allowance	3,000	—
Free domestic servant	—	3,000
Entertainment allowance	6,000	6,000
Club facility	—	6,000
Conveyance allowance for private purposes	3,000	—
Free car facility for private purposes	—	3,000
Allowance for gas, electricity and water supply	1,000	—
Free gas, electricity and water supply	—	1,000
Free holidays home facility	2,000	2,000
A rent-free unfurnished house: Fair Rent	6,000	6,000

Which of the two alternative Mr. Gupta should opt for

Solution

Computation of salary Income of Mr. A.K. Gupta for the Assessment year 1997-98

[Not covered u/s 17(2) (*iii*) in case II only]

	I	II
	Rs.	Rs.
Basic pay	20,000	20,000
Bonus	2,000	2,000
Education Allowance [Rs. 3,200 – 1,200 (50 × 2 × 12)]	2,000	—
Education Facilities—Taxable u/s 17(2)(*iii*)	—	Exempted
Club Facility	—	Exempted
Servant Allowance	3,000	—
Free domestic servant	—	Exempted
Entertainment Allowance	6,000	6,000

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	I	II
Conveyance Allowance	3,000	—
Free car [Not taxable]	—	—
Allowance for gas, electricity and water	1,000	—
Free gas, electricity and water	—	Exempted
Free holiday home facility	2,000	Exempted
Rent Free House (See Note 2)	3,700	2,800
Gross Salary	42,700	30,800
Standard Deduction u/s 16(*i*) = 33$^1/_3$%	14,233	10,267
Salary Income	28,467	20,533

Note : 1. Mr. Gupta is not covered u/s 17(2)(*iii*) i.e. specified case because his monetary emoluments less standard deduction do not exceed Rs. 24,000 in case II only.

Note : 2. Value of rent free house at chandigarh

Alternative I		*Alternative II*	
Fair Rental value =	Rs. 6,000	Fair Rental value = Rs. 6,000	
Salary [20,000 + 2,000 + 2,000 + 3,000 + 6,000 + 3,000 + 1,000] = 37,000		Salary [20,000 + 2,000 + 6,000] = 28,000	
10% of salary =	3,700	10% of salary =	2,800
Add F.R.V. (–) 50% of salary [6,000 – 18,500] =	NIL	Add F.R.V. – 50% of salary [6,000 – 14,000] =	NIL
Value	3,700	Value	2,800

Note : 3. He should opt for 2nd alternative as his salary income is less as compared to first alternative.

Illustration. 33.

(*a*) Mr. Verma has furnished following information about his income :

	Rs.
(*i*) Salary	1,500 p.m.
(*ii*) Bonus	3,000 p.a.
(*iii*) Commission	6,000 p.a.
(*iv*) Entertainment Allowance	6,000 p.a.
(*v*) Employer's Contribution to R.P.F.	6,000 p.a.
(*vi*) Value of free lunch given by employer	3,000 p.a.

Compute his salary income for the assessment year 1996-97.

(*b*) What difference it would make if

(*i*) He gets lunch allowance of Rs. 3,000 p.a. instead of free lunch; or

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(*ii*) He gets free lunch as director of the company in which he is working.

Solution. *Computation of salary income of Mr. Verma*

Particulars		Rs.
(*a*) *If free lunch given*		
salary @ 1,500 p.m.		18,000
Bonus		3,000
Commission		6,000
Entertainment Allowance		6,000
Total monetary emoluments		33,000
Employer's contribution to R.P.F.	6,000	
Less 10% of salary	1,800	4,200
		37,200
Value of free lunch—not taxable as employee is not covered under specified cases u/s 17(2)(*iii*) as his salary does not exceed Rs. 24,000 [33,000 less 1/3rd standard deduction = 22,000] and he is neither a director nor he holds 20% of more shares		NIL
Gross salary		37,200
Standard Deduction u/s 16(*i*) $33^1/_3$%		12,400
Salary Income		24,800
(*b*) (*i*) *If he gets lunch allowance*		
Total Monetary Emoluments (as per above)		33,000
Employer's contributions to R.P.F.	6,000	
Less 10% of salary	1,800	4,200
Lunch allowance—fully taxable irrespective of the status or salary		3,000
Gross salary		40,200
Standard Deduction u/s 16(*i*)—$33^1/_3$%		13,400
Salary income		26,800
(*b*) (*ii*) *If he gets free lunch as director of a company*		
Total monetary Emoluments		33,000
Employer's contribution to R.P.F.	6,000	
Less 10% of salary	1,800	4,200

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Free lunch—Taxable as he is covered under specified cases—section 17(2)(*iii*) being director	3,000
Gross salary	40,200
Standard Deduction u/s 16(*i*) : $33^1/_3$% of gross salary	13,400
Salary Income	26,800

Q. No. 14

B, a Junior Accountant drawing a salary of Rs. 2,000 per month, was made a Senior Accountant on July 1, 1994 at an increased salary of Rs. 2,200 per month. He made a petition for a much higher salary to the management on July 1, 1994 but the latter took a decision in the matter only in June 1995 when his salary was increased with retrospective effect from July 1, 1995 to Rs. 2,500 per month. The arrears of salary were drawn by B on June 30, 1996. State giving reasons the point or points of time when such arrears of salary should be considered to have accrued as income for purposes of income-tax assessment.

[**Hints:** u/s 15(c) arrears are taxable in the year of receipt as such amount of arrears received by Mr. B is income of the previous year 1996-97. Refer case *C.I.T. v. Gajapathy Naidu (1964) 53 I.T.R. 114 (S.C.)*].

Q. No. 15

Mr. X, an Indian Citizen, who was working in a University as professor, was deputed to Indian High Commission in London for a period of 3 years from 1st April 1996. He is to get a salary of Rs. 3,500 p.m., House Rent Allowance @ Rs. 1,500 p.m. and actual air fare from Delhi to London Rs. 6,000. He left Delhi on 25th March 1996 for London and was paid his air fare there in U.K. Throughout the year 1996-97 he remained in London.

Calculate his income taxable under the head 'Salaries' for the assessment year 1997-98. *[Adapted C.U. B.Com., (Hons.)]*

[**Hints:** Salary Income Rs. 28,000. H.R.A. and Air fare fully exempted u/s 10(7). [P-21.]

Q. No. 16

(*a*) Mr. B was an employee of Ray and Nath after 42 years of service retired on 28-2-1997. He was drawing a monthly salary (due on 1st of every month) of Rs. 5,000 in 1994, Rs. 5,500 in 1995 and Rs. 6,000 from 1.1.96 on wards. On retirement he received a gratuity of Rs. 1,26,000. Determine the taxable amount of gratuity. *(C.A. Inter May 1990)*

(*b*) Krishna was an employee of a public sector undertaking and retired voluntarily from its services on 31.10.96 when he was paid Rs. 4,00,000 under a scheme approved by the Central Govt. State whether it is taxable or exempted.

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(*c*) A, State Govt. servant gets absorbed on 1.6.96 in a public sector undertaking. He excercises his option to receive a lump sum in lieu of payment of pension and commutes 1/3rd of his pension rights for Rs. 2,40,000 which he received on 30.11.96. Is this receipt taxable, if so to what extent ?

[**Hints :** (*a*) Exempted gratuity Rs. 1,26,000 (*b*) Exempted u/s 10 (10 C) (*c*) Exempted u/s 10 (10 A)]

Q. No. 17

(*a*) X retires from PQR (P) Ltd. on March 31, 1996. PQR (P) Ltd. pays Rs. 800 per month as pension but does not pay any gratuity. On the request of X, PQR (P) Ltd., pays Rs. 10,000 in lieu of commutation of 20 percent of pension with effect from February 1,1997.

What is the amount of pension which is taxable for the assessment year 1997-98 if his pension is paid on last date of month.

Can the recipient claim standard deduction ?

[Company Secretary Inter June, 1993]

(*b*) X, not being covered by the Payment of Gratuity Act, 1972, retires on 6.1.1997 from PQR Ltd. and receives Rs. 46,000 as gratuity after service of 29 years and 11 months. His average monthly salary during 1.3.1996 to 31.12.96 Rs. 2,500. Determine the amount of gratuity exempt from tax for the assessment year 1997-98. *[Company Secretary Inter Dec. 1991]*

(*c*) X, an employee of ABC Ltd., receives Rs. 26,500 as gratuity under the Payment of Gratuity Act, 1972. He retires on November 13, 1996 after rendering service of 34 years and 4 months. At the time of retirement his monthly salary was. Rs. 1,352 (inclusive of dearness allowance of Rs. 100 per month).

Calculate the amount of gratuity chargeable to tax

[Company Secretary Inter Dec. 1992]

[**Hints :** (*a*) Pension Rs. 8,000 + noncommuted pension for 2 months Rs. 1,280 + Commuted value of pension—Nil (fully exempted). Standard Deduction Rs. 3,093.

(*b*) Exempted gratuity Rs. 36,250 Taxable Rs. 9,750

(*c*) Exempted gratuity Rs. 26,500] [P-28]

Q. No. 18

The following are the particulars of the income of Sh. Arvind for the previous year ending on 31st March :

(*i*) Salary Rs. 5,000 p.m.

(*ii*) Contribution to recognised P.F. Rs. 750 per month.

(*iii*) Employer contributes the same amount as the employee contributes towards P.F.

(*iv*) Dearness Allowance: Rs. 300 p.m. It is not considered for computation of his retirement benefits.

(*v*) Interest credited to P.F. @ 9% is Rs.10,000.

(*vi*) Contribution to Public Provident Fund is Rs. 12,000.

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(*vii*) Premium of Life Policy is Rs. 12,000 on a Policy of Rs. 1,00,000.

(*viii*) Deposited Rs. 1,800 in 15 years cumulative time deposit Scheme of Post Office.

(*ix*) Repayment of House Building loan taken from HDFC (a Govt. agency) Rs. 10,500 during the year.

Find out taxable income of Shri Arvind for the assessment year 1997-98.

[**Hints:** Salary income: Rs. 51,600; Q.A. for rebate of tax u/s 88 Rs. 44,800]

Q. No. 19

Mr. Ravi is employed with a public limited company in Bombay on a monthly salary of Rs. 9,500. He contributes to a provident fund which is recognised by commissioner of Income Tax @ $12^1/_2\%$ of his salary. A similar amount is contributed by the employer. Interest credit to his provident fund account during the year is Rs. 2,800. The accumulated balance to his credit is Rs. 20,000. Two children of Mr. Ravi are studying in the institution run by the employer for which no fees are paid. Normal expenditure per student in such institution is Rs. 150 a month.

The assessee is provided with a rent free unfurnished accommodation owned by the employers the municipal valuation of which is 29,400 per annum. Find out his taxable salary income.

[**Hints** : Value of rent free house Rs. 11,400, salary income Rs. 117,250]

Q. No. 20

X is a pilot in NEPC airlines at Madras. He draws Rs. 12,000/- p.m. as salary, Rs. 4,000/- p.m. as D.A. (not considered for computing retirement benefits) Rs. 16,000/- bonus and Rs. 9,000/- p.a. as educational allowance. He has got two children studying in the nearby school. He is also paid a flight allowance of Rs. 4,000/- p.m. to meet his personal expenses while on duty. He has been provided with a rent-free unfurnished flat the fair rental value of which is Rs. 60,000/- p.a. Determine the taxable value of the perquisite and gross salary.

[**Hints :** Taxable flight allowance Rs. 14,400; value of rent free house Rs. 18,220 salary income Rs. 2,33,420] [P-29]

Q. No. 21

The following particulars are given by Mr. Wadekar of Bombay in respect of his annual income for the year ended 31.3.97.

(*i*) Consolidated salary till 30.9.96 at Rs. 5,500 p.m. and from 1.10.96 Rs. 6,000.

(*ii*) HRA 20% of salary.

(*iii*) Actual house rent paid Rs. 2,000 p.m. However he owns a house property which he has let out.

(*iv*) Contribution to R.P.F. by self and employer each 14% of salary.

(*v*) LIC premium paid by employer Rs. 6,000 p.a.

(*vi*) Leave Travel Allowance Received Rs. 12,500. Rs. 10,000 was incurred on travel to home district.

(*vii*) Medical expenses incurred on treatment of his uncle Rs. 5,000. His employers reimbursed Rs. 3,000.

Compute his salary income if salary is due on last date of month.

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[**Hints :** Medical Expenses on treatment of uncle taxable; House Rent Allowance taxable Nil; Salary income Rs. 68,260 and QA for rebate u/s 88 Rs. 15,660] [P-33]

Q. No. 22

A, a resident and ordinarily resident individual, gives the following particulars of his income earned during the year ended 31st March.

(*i*)	Net salary received in hand	Rs. 25,000
(*ii*)	Tax deducted at source by employer	Rs. 2,000
(*iii*)	Own contribution to a recognised P.F.	Rs. 3,400
(*iv*)	Employer's contribution to P.F.	Rs. 3,400
(*v*)	Entertainment allowance	Rs. 600 p.m.

A was given throughout the year free use of a 20 H.P. car for the purposes of employment and for private use. Expenses were met by employer.

The entertainment allowance was given for the first time in the year ending 31st March 1962 and was continued at the same amount.

Compute A's income under the head salaries.

(B.Com., P.U. and Calcutta University)

[**Hints :** Rs. 30,400 + Excess of employer's contribution to R.P.F. Rs. 360 + E.A. Rs. 7,200 + Motor car Rs. 800 p.m. Rs. 9,600 = Rs. 47,560 less Standard Deduction of Rs. 15,853 = Rs. 31,707 No deduction of E.A.]

Q. No. 23

Mr. X, Manager in Skyways (P) Ltd., Madras gives you below the details of his income for the year ended 31 March 1997.

Salary from April to March, 97 Rs. 108,000/-. Dearness Allowance (taken into account computing retirement benefits) @ Rs. 2,000/- p.m. House Rent Allowance @ Rs. 1,750/- p.m. (Mr. X is residing in his own residence). Fixed Medical Allowance @ Rs 350/- p.m.

He was provided one Motor car with above 16 h.p. which was used partly for business and partly for personal use. The running and maintenance expenses were met by employer.

His contribution to unrecognised provident fund was @ Rs. 900/- p.m. The employer contributed an equal sum. Life insurance premium paid by Mr. X during the year amount Rs. 5,000/-.

Compute his taxable salary income for 1997-98 assessment year.

[**Hints :** Salary income Rs. 1,51,800; Qualifying Amount for rebate u/s 88 Rs. 5,000] [P-30]

Q. No. 24

Reddy is a Public Relations Officer in a Ltd. Company at Hyderabad. Compute his taxable salary income for the assessment year 1997-98 from the following:

Salary @ Rs. 9,000/- p.m. Dearness Allowance @ 2,000/- p.m. Conveyance Allowance Rs. 2,250/- p.m. the 50% amount of which he has spent for official purposes. Entertainment expenses incurred by him and reimbursed by company Rs. 6,000/-. During the year company expended Rs. 12,000/- towards his pursuing diploma course in Public relations. He has been provided with one furnished accommodation the annual fair rental value of which was Rs. 66,000/-. The cost of furniture provided at the accommodation was Rs. 30,000/-.

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Mr. Reddy contributed to recognised provident fund at 16% of his salary. Equal amount was contributed by the company. He paid life insurance premia of Rs. 9,000/- on the policy of his wife who is employed in a Government undertaking.

[**Hints :** Value of rent free house Rs. 20,400; salary income Rs. 1,57,380; Education and entertainment expenses are exempted] [P-32]

Q. No. 25

Following details are available from Sh. P.N. Dutta, a resident individual for the year ending on 31.3.97. You are required to compute his taxable income under the head 'Salaries'.

		Rs.
(*a*)	Salary received	17,800
(*b*)	Income-tax deducted at source	1,200
(*c*)	Own contribution to R.P.F. deducted from salary	2,000
(*d*)	Dearness allowance 100% of salary	
(*e*)	Employer's contribution to R.P.F.	2,000
(*f*)	Interest on accumulated balance of R.P.F. @ 9%	2,250

(*g*) He is provided with a furnished free quarter for residential purposes in Calcutta by his employer, the fair rent of which is estimated at Rs. 1,200 p.m. Cost of Furnishing is Rs. 15,000.

(*h*) He is provided with a car of 16 H.P. by his employer for both personal and official use and expenses of maintaining and running the car with chauffeur are borne by the employer.

(*i*) He had two life insurance policies: one on his own life for a policy value of Rs. 30,000 on which annual premium paid by his *employer* is Rs. 3,200; and other on the life of his wife for a policy value of Rs. 20,000 on which premium paid by him is Rs. 1,800.

Compute his total income and Q.A. for rebate u/s 88.

[Calcutta University B.Com., (Hons.) 1980]

[**Hints:** Value of rent-free house Rs. 5,400; Gross salary Rs. 61,400: Deduction u/s 16(i) Rs. 15,000; Salary Income Rs. 46,400 Q.A. for rebate u/s 88 Rs. 7,000]. [P-9]

Q. No. 26

Mr. P. Chaudhary is employed in a firm of Calcutta and he furnishes the following particulars of income for the assessment year 1997-98 :

		Rs.
(*a*)	Salary received after deduction of his own contribution to R.P.F. and income-tax at source	18,000
(*b*)	Income-tax deducted at source	1,800
(*c*)	Own contribution to R.P.F.	2,200
(*d*)	Employer's contribution to R.P.F.	2,200
(*e*)	Dearness allowance at 50% of Rs. 10,000 and 25% of the remaining basic salary per year.	
(*f*)	Interest credited to R.P.F. @ 10% p.a.	1,200
(*g*)	House rent allowance per annum (Rent paid is Rs. 750 p.m.)	8,400

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(*h*) Free lunch during office hours, the cost of which is estimated at Rs. 100 p.m.

(*i*) Conveyance Allowance [He does not spend anything] 1,800

(*j*) Premium paid on his own life policy of Rs. 45,000 5,000

Compute his total income. *[Calcutta University B.Com., (Hons.)]*

[**Hints:** Salary Rs. 22,000, Gross Salary Rs. 33,400, Deduction u/s 16(i) Rs. 11,133; Total Income Rs. 22,267 Q.A. for rebate of tax u/s 88 Rs. 7,200. Free lunch is exempted as he is not covered u/s 17 (2) (*iii*).]

Q. No. 27

Mr. Naidu was the General Manager of F Ltd. He retired voluntarily on 31.10.1996 after 20 years of service.

Following information is available:

1. Salary Rs. 6,000 per month from 1.1.95, HRA Rs. 2,000 p.m. from 1.1.95. He lives in his own house.
2. An Ambassador car (14 HP) is provided by F Ltd. for official and personal use and all expenses of its running and maintenance and salary of a driver all borne by F. Ltd.
3. He contributes 10% of salary to recognised provident fund regularly and another 10% to voluntary provident fund. The company contributes 15% of salary towards the provident fund.
4. He has invested Rs. 10,000 in National Savings certificates (VIII issue) and Rs. 20,000 in public provident fund. He paid Rs. 7,000 towards life insurance premium on a policy for a sum assured of Rs. 50,000.
5. Payment of club bills to the extent of Rs. 600 for the year, being monthly subscription @ Rs. 75/- p.m., was reimbursed by F Ltd.
6. The company provided a sweeper, a gardener and a watchman to him. Their monthly salary, paid by the company was Rs. 200 p.m. each.
7. The company paid Rs. 6,000 to gas service company for the use of cooking gas by Mr. Naidu it was the usual practice of the company to hold its business dinners in his house.
8. He received Rs. 90,000 as gratuity.
9. He received Rs. 60,000 for encashment of leave being 10 months earned leave not availed of. As per the rules of the company he was entitled to one month's leave for every year of service. During his service he has availed 10 months earned leave.

Compute his salary income for assessment year 1997-98 if salary is due on (*a*) first day of every month; and (*b*) on last date of every month.

[**Hints :** (*a*) Salary and allowances for 8 months, taxable value for servants @ 120/- p.m. per person, taxable gas bill Rs. 3,000 ($6^1/_4$%); gratuity taxable Rs. 30,000; Taxable leave encashment Rs. 12,000; salary income Rs. 1,07,080.

(*b*) Salary and allowances for 7 months; taxable gas bill Rs. 2625 ($6^1/_4$%) salary income Rs. 97,145] [P-37]

Q. No. 28

Calculate the total income of the assessee from the particulars given below for the previous year ending on March 31, 1997.

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(*i*) Mr. X receives Rs.50,000 as basic pay, Rs. 4,800 as bonus and Rs. 5,000 as D.A. (which forms part of salary for computation of service benefits).

(*ii*) He received 1% as commission on sales and sales during this period amounted to Rs. 7,00,000.

(*iii*) He and his employer contribute Rs. 600 p.m. each towards a provident fund.

(*iv*) His savings are as follows:

(*a*) Insurance premium on his own life Rs. 7,000 on a policy of Rs. 60,000.

(*b*) Contribution to P.P.F. Rs. 4,000.

(*c*) National Saving Certificates (VIII issue) Rs. 2,000.

Calculate his total income if provident fund is (*a*) S.P.F. (*b*) R.P.F. (*c*) U.R.P.F.

[**Hints:** If S.P.F. Total Income Rs. 51,800, Q.A. for Rebate u/s 88 Rs. 20,200; If R.P.F. Total Income Rs. 53,500 Q.A. for Rebate u/s 88, 20,200; If U.R.P.F. Total Income Rs. 51,800. Q.A. for Rebate u/s 88 Rs. 13,000].

Q. No. 29

A public limited company at CALICUT is paying the following salary and allowances to its chief executive:

(*a*) Salary Rs. 4,500 p.m.

(*b*) Conveyance Allowance Rs. 500 p.m. He spends whole of this amount in the performance of his duties.

(*c*) Dearness allowance of Rs. 400 p.m. (Enters into pay for service benefits).

(*d*) Entertainment allowance of Rs. 500 p.m. The assessee claims that the entire amount is spent by him on entertaining company's guests.

(*e*) Medical expenses upto Rs. 5,000 are reimbursed by the employer on production of bills.

(*f*) He stays in a bungalow in the immediate vicinity of the office. Rent payable by the company for this house is Rs. 36,000 p.a. His stay in the house is necessary and in the interest of the company.

The employee is married and is having three children and during the previous year he is paid leave travel concession of Rs. 10,000 for going to Kashmir with his family.

You are required to compute his salary income for the assessment year 1997-98.

[Calicut University M.Com., April 1981]

[**Hints:** Conveyance allowance fully exempted; Entertainment allowance fully taxable; Gross Salary Rs. 74,880, Salary Income 59,880].

Q. No. 30

Dr. A.B. Mukerjee was appointed as Principal of Govt. College on 1.1.94 in the Grade of Rs. 3,700 – 125 – 4,950 – 150 – 5,700 at a basic pay of Rs. 3,700 p.m. He is getting D.A. of Rs. 4,805/- p.m. He is receiving C.C.A. @ Rs. 100 p.m. He is contributing Rs. 400 p.m. to provident fund. Interest credited to provident fund account is Rs. 6,000.

He is provided with rent-free house whose rental value is Rs. 200 p.m. He received Rs. 2,400 as remuneration for acting as controller of examinations on behalf of University.

He had paid contribution to Unit Linked Insurance Plan of Rs. 2,400 and to P.P.F. Rs. 4,000.

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Compute his Total Income for the Assessment year 1997-98.

[**Hints:** Basic Salary as on 1.1.96 Rs. 3,950 p.m. 1.1.97 Rs. 4,075 p.m. (Salary due on 1st of every month), value of rent-free house 2,400: Salary income Rs. 93,910 Total Income 96,310 Q.A. for rebate u/s 88 Rs. 11,200. Provident Fund is S.P.F.] [P-10].

Q. No. 31

Shri Radha Raman Raha furnishes you with the following particulars with a request to compute his total income for the year ending on 31st March, on the basis of which he will submit his return of income to the income-tax authorities:

(*a*) Salary Rs. 3,000 p.m.

(*b*) Annual Profit Bonus paid in February—20% of salary.

(*c*) He was provided with a rent-free accommodation in Calcutta for which a rent of Rs. 750 was paid monthly by his employer.

(*d*) His life insurance premium of Rs. 6,000 was paid by his employer in March 1997.

(*e*) His wife was sick and medical expenses amounting to Rs. 16,000 were paid by his employer in January, 1997. Treatment was taken from a private hospital.

(*f*) He was provided with a domestic servant whose monthly salary of Rs. 100 was paid by his employer.

(*g*) He purchased books and Engineering journal valuing Rs. 1,252 in September, 1996.

(*h*) Rs. 3,000 was paid by his employer in July towards reimbursement of tution fee of his eldest son.

(*i*) He paid 10% of salary towards R.P.F. *(Adapted I.C.W.A.)*

[**Hints:** Value of rent-free accommodation Rs. 4,320; Net salary being T.I. Rs. 48,720; Q.A. for rebate u/s 88; Rs. 9,600; Tuition fee reimbursed by employer is fully taxable.]

Q. No. 32

From the particulars given below, compute the total income of Sh. P.M. Dave, executive officer in a company in Bombay.

Pay @ Rs. 2,500 p.m.

D.A. @ Rs. 500 p.m. (Enters into pay for service benefits).

Provided with rent-free 5 room house fully furnished, the Fair Rental Value being Rs. 2,000 p.m. Cost of furnishing Rs. 30,000 which includes expenditure on furnishing a room Rs. 10,000. This room is used by the officer for his employment purposes only.

His and employer's contribution to R.P.F. @ $12^1/_2$% of salary. Other benefits are:

(*i*) Telephone Bill Rs. 2,500 (Telephone was installed at his residence for his use).

(*ii*) Club Bill paid by employer Rs. 4,100.

(*iii*) Education Allowance Rs. 2,700. (His two children are studying in school).

(*iv*) Reimbursement of Medical Bills Rs. 1,555.

(*v*) He is provided with a car of 14 H.P. which he uses exclusively for employment purposes.

(*vi*) Leave Travel Concession for going to a Hill Station Rs. 4,500.

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[**Hints:** Value of rent-free house 5,750; Leave Travel Concession. Telephone Bill & medical reimbursement tax-free. Gross Salary Rs. 48,250; Standard Deduction Rs. 16,083; Salary income Rs. 32,167; Q.A. for rebate u/s 88 Rs. 4,500; Education allowance exempted Rs. 1,200] (P-14).

Q. No. 33

Mr. Rehman is a professor in a College, at Bombay. His salary particulars are as follows:

	Rs.
Basic pay in April 96 [Salary due on last date of month	9,000/- p.m.
Annual increment [Rs. 250) due on 1st June 96 D.A. (enters)	1,200/- p.m.
Warden allowance	500/- p.m.

The college has provided Mr. Rehman a free furnished accommodation. The fair rental value of the house is Rs. 4,000 p.m. He has also been provided with a gardener, a sweeper and a watchman whose monthly salaries are Rs. 600, Rs. 500 and Rs. 650 respectively. A free telephone has been installed in his house. He uses the phone both for official and personal purposes.

He spent Rs. 40,000 on a operation on his son performed in a hospital in New York where his another son resides. The managing committee of the college, as a special case reimbursed Rs. 30,000 towards the above expenses. R.B.I. allowed foreign exchange upto Rs. 25,000.

He is a member of a provident fund maintained by the college. He contributes 12% of his salary as compulsory contribution and 10% thereof as voluntary contribution. The college contributes to his PF 10% of his salary.

He was allotted a flat in April 96 by the Bombay Housing Board under self financing scheme. To meet the cost of the house he had borrowed Rs. 1,00,000 from college and Rs. 50,000 from Housing Development Finance Corporation. During the previous year the loan and interest repayments are as follows :

	Loan	Interest
HDFC	Rs. 5,000	Rs. 1,800
College	Rs. 10,000	Rs. 3,200

Mrs. Rehman had taken out a policy for Rs. 60,000 on son's life for which she paid a premium of Rs. 8,000 during this previous year.

Compute his salary income for the assessment year 1997-98.

[**Hints :** Salary Rs. 1,10,500; servants taxable @ 120 p.m. per person; medical expenses taxable Rs. 5,000; Free Telephone exempted; Rent free house Rs. 13,090; salary income Rs. 1,36,870; Q.A. for rebate u/s 88 Rs. 37,478] [P-35]

Q. No. 34

Shri Sukhwasi is Secretary to Hamesha Nuksan Ltd., and for the period between 1.4.1996 and 31.3.1997 has received the following salary and other payments from his company.

	Rs.
(*i*) Salary	@ 2,000 p.m.
(*ii*) Dearness allowance	@ 250 p.m.
(*iii*) City compensatory allowance	@ 100 p.m.

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(*iv*)	Entertainment allowance (received from 1.4.1952 in a company which was amalgamated with Hamesha Nuksan Ltd. with effect from 1.4.1970)	@ 7,200 p.a.
(*v*)	Commission on sales achieved by him	3,000
(*vi*)	Rent-free accommodation of a building (furnished) which pays a municipal tax on Rs. 16,000 per annum and furniture value is Rs. 20,000.	
(*vii*)	Medical bills reimbursed by company	2,000

Shri Sukhwasi contributed Rs. 7,500 to a recognized provident fund. He also paid life insurance premium of Rs. 960 on the life of his son. He seeks your advice in preparing the return. What guidance would you give him ? What is the salary income on which he is assessable?

[**Hints:** Gross Salary Rs. 48,960; Deductions u/s 16(*i*) Rs. 16,320 & 16(*ii*) Rs. 4,800; Salary Income & Total Income Rs. 27,840; Q.A. for rebate u/s 88 Rs. 8,460. Value of Rent-free house Rs. 5,560].

Q. No. 35

Mr. Vivek is employed in a company of Calcutta on a salary of Rs. 5,000 p.m. He contributes 12% of his salary to the company's provident fund recognised under the Income-tax Act and a similar amount is contributed by the company. Interest of Rs. 2,240 was credited to his account in the fund during the year, on a credit balance of Rs. 28,000. He has been provided with a house for his residence free of rent; the house is owned by the company and the Municipal valuation of the same is Rs. 7,800 p.a. The company has furnished the house at a cost of Rs. 20,000. He is also provided with a car (14 h.p. rating) for his use at the company's expense, on condition that he will meet its running and maintenance charges to the extent of private and personal use. The company has engaged a driver for the car on a salary of Rs. 450 p.m. The company meets the personal expenses of Mr. Vivek's two children amounting to Rs. 3,600 p.a. and also paid the premium, amounting to Rs. 2,600 per year on an insurance policy for Rs. 50,000 on Mr. Vivek's life, Mr. Vivek has, in addition, two multipurpose policies of Rs. 25,000 each on the lives of his two children, for which, he pays yearly premium of Rs. 800 each. Compute Mr. Vivek's total income.

[Adapted Company Secretaries]

[**Hints:** Value of rent-free house Rs. 8,000; Car Perk Rs. 2,400 + Rs. 3,600, Gross Salary Rs. 81,400; Standard Deduction Rs. 15,000; Total Income Rs. 66,400 Q.A. for rebate u/s 88 Rs. 11,400 (P-15)].

Q. No. 36

Mr. C.K. Tata was the executive director of XY. Co. Ltd., a company having its head office at Kanpur and branches at Bombay and Calcutta. His contract of employment was for a period of three years. For the year he submitted the following return:

		Rs.
(*i*)	Salary @ Rs. 3,000 p.m.	36,000
(*ii*)	Conveyance allowance @ Rs. 300 p.m.	3,600

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(*iii*) Education allowance for the child @ Rs. 250 p.m.			3,000
(*iv*) Club Bills reimbursed by the Company			1,200
			43,800
		Rs.	
Less: (*a*) Maintenance and wear and tear of his car used for official duties		2,000	
(*b*) Entertainment expenses incurred on the customers		2,000	
(*c*) Donation to Gandhi Memorial Fund		1,000	
(*d*) Expenses on education of his son		2,000	
			7,000
			36,800

The following particulars are available on record:

(*i*) Mr. Tata has kept in his occupation free of rent half portion of the company's premises at Bombay. Annual rent of the building is Rs. 24,000.

(*ii*) He has contributed Rs. 6,000 to a Recognised Provident Fund and has paid premium amounting to Rs. 5,000 on a policy of Rs. 40,000.

(*iii*) He took an advance salary of Rs. 9,000 in March 1997.

Work out his income from salary and the qualifying amount for rebate u/s 88. *[Adopted B.Com., Punjab]*

[**Hints :** Gross Salary Rs. 54,200; Standard Deduction Rs. 18,000; Salary Income Rs. 36,200; Education Allowance Exempted Rs. 600. Qualifying amount Rs. 11,000] [P-13].

Q. No. 37

Mr. Ghosh is the Chairman of Indian Tobacco Co., Ltd., Calcutta. His salary and other particulars for the year ending 31.3.97 are as follows:

	Rs.
Salary	60,000/- p.m.
D.A. (not considered for retirement benefits.)	10,000/- p.m.
Bonus for the year	72,000/-
Arrears of earlier year's bonus	10,000/-
Commission on profits for 96-97	80,000/-
Advance salary for April 97 drawn in March 97	60,000/-
Employer's contribution to recognised provident fund	12% of salary
Profession tax paid by the company	2,000/- P.A.
Income tax paid by the company	15,000/- p.m.
Electricity bills for the year paid by the company	8,000/-
Fees for attending board meetings.	13,000/-

The company has provided Mr. Ghosh a contessa car (18 H.P.) which is used by him both for official and personal purposes. The entire running and maintenance cost amounting to Rs. 45,000/- for the year has been met by the company. His

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two children are studying in Doon School. Dehradun the education expenses during the year being Rs. 40,000/- fully met by the company.

He has also been given a spacious bungalow free of rent. The company owns the bungalow. The fair rental value of the bungalow is Rs. 18,000/- p.m.

There is a swimming pool inside the bungalow compound the maintenance cost of which came to Rs. 20,000/- for this year. The company met it.

The garden inside the compound wall is maintained by the company. The gardener is paid a salary of Rs. 1,000/- p.a. The maintenance cost came to Rs. 6,000/- during the year.

The chairman has also been provided with a security and a sweeper whose salaries ammounting respectively to Rs. 1,600/- p.m. and Rs. 1,500/- p.m. have been paid by the company.

The entire bungalow is richly furnished with furniture costing Rs. 4,50,000/-

Determine salary income and also the perquisite value of the rent-free bungalow in the hands of Mr. Ghosh.

[**Hints :** Value of rent free house Rs. 1,50,400 salary income Rs. 14,52,280] [P-38]

Q. No. 38

A, a resident individual, is serving in X Ltd., New Delhi, and furnishes the following particulars of his income earned during the year ended on 31st March.

	Rs.
Salary	60,000
His own contribution to a R.P.F.	8,000
Employer's contribution to the said Fund	8,000
Bonus (Gratutious)	5,000

(*i*) He is provided with a 14.5 H.P. motor car which is owned by the employer, all the expenses of maintenance and running met by the employer. He is also provided with a driver for the said car for which no charge is made to him by the employer. Mr. A uses the car for his personal purposes also.

(*ii*) L.I.C. premium paid by the employer amounting to Rs. 5,000.

(*iii*) He is provided with rent-free unfurnished accommodation, the fair rental value of which is Rs. 20,000 per annum.

Compute his total income.

[**Hints:** Salary Income Rs. 73,800; Q.A. for rebate u/s 88 Rs. 13,000; Value of rent-free house Rs. 6,000].

Q. No. 39

From the following particulars of the income of Mr. P, a senior officer in D.C.M. Ltd., Delhi since 1950, compute his total income for the year ending 31st March, 1997 :

(*a*) Basic Salary, Rs. 50,000.
(*b*) City compensatory allowance, 20% of salary.
(*c*) Entertainment allowance, Rs. 5,000.
(*d*) Conveyance allowance, Rs. 6,000.
(*e*) Family allowance, Rs. 3,000.

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(*f*) Profit Bonus @ 20% of salary.

(*g*) Rent-free unfurnished accommodation of a fair rental value of Rs. 6,000 p.a.

The other particulars are:

(*i*) He contributes 12% to an unrecognised provident fund.

(*ii*) Pays life insurance premium amounting to Rs. 5,000, the capital sum assured being Rs. 40,000.

(*iii*) 75% of the conveyance allowance was stated to have been spent in discharging official duties.

(*iv*) Prior to 1st April, 1955, Mr. P used to get entertainment allowance—Rs. 300 p.m. *(Adapted B.Com. Delhi University)*

[**Hints :** Gross Salary Rs. 85,500; Standard Deduction Rs. 15,000; Entertainment Allowance Deduction Rs. 3,600; Salary Income Rs. 66,900; Q.A. for rebate u/s 88 Rs. 5,000; Value of Perk is only Rs. 6,000].

Q. No. 40

Mr. A.K. Verma was working as Manager at Rs. 7,200 p.m. with Hindustan Photo Ltd., Jammu. He was receiving Rs. 1,800 p.m. as D.A. and Rs. 3,000 p.m. as House Rent Allowance. He stays in his own house. He received Rs. 14,000 as travelling allowance and he could spend only Rs. 12,500. His salary accrues on 1st day of every month.

He retired from service with effect from Jan. 31, 1997 and received the following amounts:

(*i*) Retirement Gratuity Rs. 1,62,400. He retired after rendering 34 years' service and his salary during 1996-97 was Rs. 7,200 p.m.

(*ii*) His pension was fixed @ Rs. 2,800 p.m. He gets 3/4th of his pension commuted for a lump sum of Rs. 2,10,000.

(*iii*) He received Rs. 1,24,000 as refund from Recognised Provident Fund. Half of it consists of his own contribution plus interest thereon.

(*iv*) Leave Encashment of Rs. 36,000 being 5 months' salary received on 31.1.97. He was allowed one month leave for each year of service.

Compute his salary income for the previous year ending on March 31, 1997.

[**Hints:** Taxable Gratuity Rs. 40,000; Taxable commuted value of Pension Rs. 1,16,667. Taxable Pension Rs. 700; Salary Income Rs. 2,75,867; R.P.F. Balance exempted] [P-5].

Q. No. 41

Sh. J.K. Jain is working at Chandigarh. For the year ending 31.3.97 he has furnished the following particulars of his income:

(*i*) Pay Rs. 2,500 p.m.; (*ii*) Dearness Allowance @ Rs. 400 p.m. (out of this Rs. 200 p.m. enter into pay for service benefits); (*iii*) Advance Salary Rs. 5,400; (*iv*) Salary in lieu of leave Rs. 3,000; (*v*) Lunch Allowance @ Rs. 200 p.m.; (*vi*) He was given a gift of refrigerator costing Rs. 8,000 during the year in appreciation of services; (*vii*) Employee & Employer's contribution to R.P.F. @ 15% (each) of salary; (*viii*) Arrears of D.A. Rs. 300; (*ix*) Conveyance allowance received during the year Rs. 2,500 and he has incurred an expenditure of Rs. 1,800 during the year on conveyance; (*x*) House Rent allowance 20% of Salary. He pays rent of

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Rs. 600 p.m. (*xi*) He receives Rs. 500 p.m. as entertainment allowance. Before 1.4.55 he was getting Rs. 250 p.m. as entertainment allowance from same employer. Compute his Salary Income.

[**Hints:** Gross Salary Rs. 64,740; Standard Deduction Rs. 15,000; Deduction u/s 16(ii) E.A. Rs. 3,000; Salary Income Rs. 46,740; Lunch Allowance is fully Taxable. Taxable H.R.A. Rs. 2,520; D.A. enters into pay for all purposes] [P-6].

Q. No. 42

From the particulars given below compute his salary income:

(*i*) Basic Salary Rs. 3,000 p.m.

(*ii*) Dearness Allowance Rs. 900 p.m. (Rs. 500 p.m. enters into pay for service benefits).

(*iii*) Bonus @ 20% of salary p.a.

(*iv*) Salary in lieu of leave Rs. 3,000.

(*v*) Entertainment allowance Rs. 1,500 p.m. (Before 1.4.55 Rs. 900 p.m.).

(*vi*) Reimbursement of Conveyance expenditure incurred in performance of duties Rs. 200 p.m.

(*vii*) Furnished House at Concessional rent of Rs. 800 p.m. in Madras Fair Rental Value Rs. 2,500 p.m. Cost of furniture Rs. 35,000. Salary of gardener Rs. 1,000 p.a.

(*viii*) Club bill paid by employer Rs. 2,200 p.a.

(*ix*) Contribution by employee and employer to R.P.F.—12% (each) of salary.

(*x*) Reimbursement of Medical Exp. Rs. 2,000.

(*xi*) Life Insurance Premium (Paid by employee)

own life = 3,000 p.a.
wife's life = 4,000 p.a.
major son = 2,000 p.a.

(*xii*) C.T.D. payment Rs. 200 p.m. in 10 year A/c.

(*xiii*) Contribution to Public P.F. Rs. 2,000 p.a.

[**Hints:** Gross Salary Rs. 79,260; Standard Deduction u/s 16(i) Rs. 15,000; Entertainment allowance deduction Rs. 7,200. Salary income being Total Income = Rs. 57,060; Value of Concessional rent Accommodation Rs. 20. Salary for this purpose Rs. (36,000 + 6,000 + 8,400 + 10,800). Q.A. for rebate u/s 88 Rs. 18,440] [P-18].

Q. No. 43

X, an employee of the Gas Supply Limited, Agra receives the following emoluments during the previous year 1996-97:

	Rs.
Basic pay	10,000 p.a.
Project allowance	1,800 p.a.
Arrears of project allowance of May, 1995	150
Professional tax paid by the employer	200 p.a.
Rent-free furnished house	
—Fair rent of the house	5,600 p.a.
—Rent of furniture	500 p.a.

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Free gas supply	400 p.a.
Services of sweeper	2,000 p.a.
Services of gardener	1,000 p.a.
Salary of cook (*Employed by Employee*)	800 p.a.
Free lunch	2,400 p.a.
Free use of chauffeur driven Maruti car which is used partly for official and partly for private purposes.	8,000 p.a.

He is a member of a recognised provident fund to which he contributes Rs. 1,500; his employer also contributes an equal amount. He deposits Rs. 600 per annum in 10 years' account under the Post Office Saving Bank (CTD) Rules. Determine his taxable income for the assessment year 1997-98—(*a*) if X is a director in the employer company and rent-free house is owned by it, (*b*) if X is neither a director nor a shareholder in the employer company and the rent-free house is not owned by it. *[Company Secretaries Final]*

[Hints: (*a*) *If director*—Value of rent-free house Rs. 2,300. Perks of Cook, Car, free lunch and sweeper taxable, gardener's salary to be added in F.R.V.; Gross Salary Rs. 30,390; Standard Deduction Rs. 10,130. Salary Income Rs. 20,060 Q.A. for rebate u/s 88 Rs. 2,100].

(*b*) *If not director*—Value of rent-free house Rs. 1,700; Perks of gardener, Lunch, sweeper and car not taxable; Gross salary Rs. 15,150; Q.A. for rebate u/s 88 Rs. 2,100. *Perk of gas is fully exempted in both the cases.*] [P-16].

Q. No. 44

Dr. Sunil is employed as a resident doctor in XYZ Hospital Ltd. on a basic salary of Rs. 6,000 per month.

1. He is required to stay with his family in a free-unfurnished bungalow provided by his employer in hospital compound.
2. Hospital pays college fee of Rs, 3,600 during the year directly to the college for his daughter, while his son is getting free education in an institution run by the employer. His son is also given free transport to and from the school. The normal expenses on education and transport are Rs. 300 p.m.
3. A gardener and a watchman look after his bungalow. They are employees of the hospital on a salary of Rs. 400 per month each.
4. He is entitled to holiday home facility at company's guest house at Darjeeling and this had been availed by him for 15 days during the year alongwith his family. He was reimbursed the travelling expenses of Rs. 15,000 and was given free board and transport there. Rs. 6,000 are normal changes for such accomodation.
5. Since he had availed 15 days leave out of 30 days to which he was entitled, he encashed the balance leave of 15 days and got Rs. 3,000.
6. Hospital pays Rs. 1,000 per month on an accident insurance policy for the benefit of Dr. Sunil.
7. Hospital has reimbursed his fee of Rs. 1,000 per annum and Club bills aggregating Rs. 6,000 which included bills for entertaining his guests some of whom were hospital's customers.
8. He purchased a car at Rs. 90,000 (book value) from the hospital. The market value of the same is about Rs. 100,000.

Dr. Sunil had no share in the XYZ Hospital Ltd. he was not related to any director. Discuss the tax treatment that may be accorded to each of the above items in the hand of Dr. Sunil. There is no need to compute his tax.

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[**Hints :** Expenses on son's education taxable; holiday home facility taxable; Accident insurance taxable as it is for the benefit of employee, club bill and subscriptions exempted. Concession of car taxable; value of rent free house = 10% of salary; Salary income Rs. 1,03,840] [P-36]

Q. No. 45

B, a British National, came to India on June 1, 1990 taking up employment with an Indian Company with whom he was still serving. During this period of service he had been away from India on leave every year for the months of January and February. He gives the following particulars of his income for the year ending on 31st March, 1997 :

(*i*) Basic salary, dearness allowance, marriage allowance and foreign allowance at the rate of Rs. 6,000, 1,500, 1,200 and 800 p.m. respectively.

(*ii*) An unfurnished house in Calcutta for which company pays a rent of Rs. 3,200 p.m. and recovers from B Rs. 500 p.m.

(*iii*) Own contribution to a recognised provident fund @ Rs. 1,250 p.m. matched by an equal contribution by the employer.

(*iv*) Passage Money of Rs. 50,000 for self and wife for leave, to U.K. and returning therefrom.

(*v*) A 16 H.P. car for personal as well as official purposes provided by the company, running and maintenance expenses met by it.

(*vi*) Dividend of Rs. 20,000 received in U.K. from Sterling companies.

During the period he stayed away from India due to leave, he gave up rights to occupy the house provided and the use of car. B took out a policy in India, a Life Insurance Policy for a sum of Rs. 1,00,000 and paid a premium of Rs. 6,000 during the year.

Compute B's total income. *(Adapted B.Com., Calcutta)*

[**Hints:** Gross Salary Rs. 1,30,800, Value of rent-free house Rs. 3,000. Standard deduction Rs. 15,000. Total Income Rs. 1,15,800; Q.A. for rebate u/s 88 Rs. 21,000; Passage Money exempted. Dividend is not taxable as B is Resident but not ordinarily resident] [P-19].

Q. No. 46

S, a salaried employee in F Co. Ltd., and an Indian citizen, gets a salary of Rs. 3,500 p.m. He is allowed to use any of the two cars owned by his employer. One of the Cars is of 8 Hp and other is of 18 HP. He uses these cars for his official work as well as for his personal matters. The company maintains these cars. The recognised provident fund is also maintained by his employer and for the year ended on 31st March, 1997 the employer's contribution and the employee's contribution to S's provident fund account amounted to Rs. 5,250 each.

In terms of services S is required to entertain the clients of F Co. Ltd. and he gets an allowance at Rs. 750 p.m. for this purpose. He has been serving with F Co. Ltd. since 1953 and has always been in receipt of an identical allowance for entertaining clients.

The company provides him with rent-free furnished accommodation in Calcutta and pays a rent of Rs. 1,700 p.m. to the owner of such accommodation. He was provided with a gardener for the upkeep of the garden, to whom the employer paid @ Rs. 400 p.m.

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During the year ended on 31st March, 1997 Mr. S paid life insurance premium of Rs. 4,000 on a policy of Rs. 1,00,000 taken out on his own life.

Assuming that Mr. S had no income except that from his employment with F Co. Ltd. during the year ended on 31st March, 1997. Compute his total income for the Assessment Year 1997-98 and indicate whether any relief or rebate is available to him, and if so, the amount by reference to which such rebate is to be computed.

[C.U., B.Com. (Hons.)]

[**Hints:** Gross Total Salary Rs. 67,440; Salary Income Rs. 44,940; Q.A. for rebate u/s 88 Rs. 9,250] [P-22].

Q. No. 47

Mr. B Sen employed at Calcutta with a mercantile firm as Sales Manager. From the undernoted particulars, compute his taxable income for the Assessment Year 1997-98.

(*a*) Basic Salary—Rs. 2,500 × 12 = Rs. 30,000.

(*b*) Dearness Allowance at 20% of the basic salary but only 10% of salary is eligible for service benefits.

(*c*) Incentive Commission at 1% of the sale achieved by him but not exceeding 50% of monthly salary of Rs. 2,500. The turnover achieved by him for the relevant previous year before charging the said commission was Rs. 1,72,800.

(*d*) Mr. Sen's contribution to the Recognised Provident Fund of the firm is Rs. 6,000 for the year and his employer also contributes an equal amount.

(*e*) Interest credited to Provident Fund at the rate of 14% per annum amounted to Rs. 4,200.

(*f*) The employer pays Mr. Sen a house rent allowance of Rs. 700 per month and Mr. Sen lives in a rented house for which he pays a rent of Rs. 1,000 per month.

(*g*) He is provided with a motor car of more than 16 H.P. rating which he uses both for private and office purposes. All expenses of the said car including driver's salary of Rs. 1,250 per month, are paid by the employer.

(*h*) During the relevant previous year he purchased books worth Rs. 800 for his office work.

(*i*) He has been getting entertainment allowance of Rs. 8,000 per year from the same employer since 1953.

(*j*) Mr. Sen's son is a medical student of Calcutta Medical College and Mr. Sen spent Rs. 2,000 for his studies.

(*k*) According to the terms of appointment his employer contributes a sum of Rs. 6,000 per year to an approved Superannuation Fund on his account.

(*l*) During the relevant previous year Mr. Sen paid the following Life Insurance Premiums :

(*i*) On a policy of Rs. 60,000 on his own life—Rs. 7,600.

(*ii*) On a policy of Rs. 50,000 on his wife's life—Rs. 4,000.

[C.U., B.Com. (Hons.)]

[**Hints:** Salary Income Rs. 37,625; Q.A. for rebate u/s 88 Rs. 17,600] [P-23]

Q. No. 48

B, a resident of India, furnishes the under noted particulars of his income and outgoings for the purposes of assessment for the assessment year 1997-98 :

(*i*) He drew salary of Rs. 3,000 per month and dearness allowance @ 20 per cent of the salary throughout the previous year.

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(*ii*) A bonus of 4 month's basic salary was received by him, out of which one month's bonus was gratuitous and three month's was as per agreement with the labour union.

(*iii*) As a member of a recognised provident fund he contributed 10% of his salary to the fund and his employer contributed an equal amount. Interest of Rs. 3,000 calculated @ 10 per cent was credited to the provident fund account.

(*iv*) He was provided with rent-free furnished accommodation at Calcutta for which his employer paid a rent Rs. 1,000 per month. The furniture belonged to the employer of which the original cost was Rs. 20,000.

(*v*) B got a conveyance allowance of Rs. 500 per month. He owned a car which was used by him for employment purposes also. The monthly expenses for running and maintaining the car were Rs. 1,200 per month on an average of which 50 per cent is attributable to use for employment.

(*vi*) Life insurance premia of Rs. 5,000, Rs. 3,000 and Rs. 1,000 were paid by B on his own life, his wife's life and his minor son's life, the sums assured being Rs. 1,00,000, Rs. 1,00,000 and Rs. 25,000 respectively.

(*vii*) A sum of Rs. 500 per month was paid towards 10 year Cumulative Time Deposit with the Post Office.

(*viii*) B received during the year bank interest of Rs. 2,000, dividends of Rs. 2,500 (gross) from Indian companies and Rs. 1,700 on 2,000 units of Rs. 10 each in the Unit Trust of India.

Compute the Salary Income and Qualifying Amount for rebate of Mr. B for the assessment year 1997-98 on the basis of the above-noted data.

[C.U. B.Com. (Hons.)]

[**Hints:** Salary Income Rs. 46,700; Q.A. for rebate u/s 88 Rs. 18,600. Gratuitous bonus does not enter into salary for rent-free house] [P-24].

Q. No. 49

Mr. Ramamurthy furnishes the following details of his salary income :

	Rs.
1. Salary	50,000
2. Encashment of earned leave	10,000
3. Uniform allowance Spent Rs. 6,000 on purchase and maintenance of the uniform	5,000
4. Research allowance Spent on research Rs. 3,000 during the previous year	3,000
5. Scholarship granted to his son by University	4,800
6. Education allowance for his grand daughter	3,000
7. Education allowance for his son studying outside India	3,000
8. Interest free loan to buy a car Normal rate of interest is 14%	1,50,000
9. Helper allowance Engaged a helper for the performance of duties of the office and paid him Rs. 9,000	10,000
10. Professional tax paid by the employer	1,000

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11. Refereshment during office hours at an estimated cost of Rs. 200 p.m. 2,400
12. Employer paid his club bills 3,000
13. Employer's & Employee's contribution to R.P.F. is 12% of salary
14. H.R.A. received by him is Rs. 1,600 p.m. and rent paid by him is Rs. 2,000 p.m.
15. Insurance premium paid by him on his own life Rs. 6,000 assured amount is Rs. 50,000 and on the life of his wife :—

Premium is Rs. 6,000 sum assured Rs. 60,000.

Compute his taxable income for the assessment year 1997-98 and Q.A. for Rebate U/S 88.

[**Hints** : Uniform, Research and Helper Allowance exempted upto actual expenditure. Interest on Loan-exempted perk ; Salary Income Rs. 56,200. Q.A. for rebate Rs. 18,000. Education Scholorship from University is exempted] [P-20].

Q. No. 50

Mr. Arun an employee of Arun Corporation Ltd. receives the following salary and perquisites from his employer during the previous year 1996-97 :

Basic pay Rs. 75,000 pa. Profit bonus Rs. 7,500, Commission on sales @ 2 per cent of turnover (turnover of the year 1996-97 achieved by Arun Rs. 8,50,000).

Advance salary of April and May 1997 Rs. 15,000. Employer's contribution towards recognised provident fund Rs. 9,000, Interest credited on May 15, 1996 in provident fund account @ 14.5 per cent Rs. 8,700, travelling allowance Rs. 400 which is fully utilised for official purposes, a rent free furnished house in Bombay (rent of unfurnished house paid by employer Rs. 48,000, rent of furniture Rs. 12,000) free services of a Gardner (Salary Rs. 3,000), free services of Watchman (Salary Rs. 4,200), free services of Cook (Salary Rs. 3,000) and free supply of ration (expenditure of the employer Rs. 7,500). He owns a house at Madras. During the previous year he earns taxable income of Rs. 15,000 from the house.

Arun holds 20 per cent equity shares in the employer company. During the previous year Arun makes the following payments and investments :

(*a*) Own contribution towards recognised provident fund Rs. 9,000.

(*b*) Deposits in 10 year account under the Post Office Savings Bank (CTD) Rules : Rs. 13,000 (including advance deposit of Rs. 1,000).

Determine taxable salary income and qualifying amount for rebate u/s. 88.

[**Hints** : Value of rent free house Rs. 21,950.; Free ration taxable ; Salary Income Rs. 136,330 ; QA for rebate Rs. 22,000] [P-25].

Q. No. 51

Krishna is an officer of a firm at Mangalore. The details of his salary and other incomes for the previous year 1996-97 are as follows :

	Rs.
Basic Pay	60,000
D.A. (Forming part of Salary)	2,400
Education allowance for 2 Children (one of the child is in Hostel and one is day boarder)	6,000

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House Rent allowance	8,000
His own contribution to RPF	5,000
Employer's contribution to RPF	7,000
Interest credited to accumulated balance of provident fund at 14%	2,800

He is provided with the services of a cook and a watchman who are paid Rs. 200 and Rs. 400 p.m. respectively. He is also provided with a car of 14 H.P. for official and private purpose. Expenses of the car are met by the Co. He has been living in a rented house and paying Rs. 900 p.m. as rent.

He paid LIC Premium of Rs. 3,500 on his own life policy of Rs. 50,000. He deposits in 10 year Post Office Savings Bank account CTD Rs. 6,000.

Compute his salary income for the A.Y. 1997-98 and qualifying amount for rebate u/s 88. *(B.Com., Mangalore 1993)*

[**Hints** : Taxable HRA Rs. 3,440 ; Salary Income Rs. 66,040 ; Q.A. for rebate u/s 88 Rs. 14,500] [P-26]

Q. No. 52

Mrs. R.P. Sharma is employed with Jai Springs (P) Ltd. Chandigarh. She draws salary of Rs. 4,800 p.m. and D.A. Rs. 1,200 p.m. which is not a part of salary for superannuation benefits. She has been getting entertainment allowance at the rate of Rs. 700 p.m. since 1-4-54. She is paid a bonus of Rs. 12,450. At the end of March 1997, she took three months salary (basic pay + D.A.) in advance and loan of Rs. 15,000 to meet the expenses of her daughter's marriage.

She is provided with unfurnished house owned by the Company, the fair rent of which is Rs. 42,000 p.a. She has been also provided with the services of a gardener and a watchman. The Company pays Rs. 100 p.m. and Rs. 480 p.m. to them respectively. Her two children are getting free education in a school, run by the Company. The tution fee in a nearby school is Rs. 100 p.m. per head. She has been allowed the facility of a driver driven motor car of 16 H.P. for official and personal purposes. The Company also paid income-tax Rs. 4,000 on her salary.

She contributes 10% of her salary to a recognised provident fund to which the employer contributes 14%. Interest on the accumulated balance credited on 30th June, 1996 at the rate of 13% p.a. amounts to Rs. 9,100/-. She has insured her life for Rs. 60,000/- and pays Rs. 4,000/- annual premium. She also deposited Rs. 6,000/- in Public Provident Fund Account and invested Rs. 12,000/- in National Saving Certificates VIII issue.

Compute her Total Income for the assessment year 1997-98

[**Hints** : Value of rent free house Rs. 13,220 salary Income Rs. 1,23,214 ; Q.A. for rebate u/s 88 Rs. 27,760] [P-27]

QUESTIONS

1. (*a*) Define 'Salaries'.
   (*b*) Distinguish between statutory provident fund; recognized provident fund and an unrecognized provident fund. *[B.Com. Pass, Delhi]*
2. Define the term perquisite and how are they treated for income-tax purposes? *[B.Com. Hons., Delhi]*

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3. What are the important types of provident funds of which a salaried employee may be member and state the income-tax provisions dealing with each type of provident fund.
4. What rebate from income-tax is allowed to an assessee in respect of life insurance premiums and provident fund contributions and interest thereon and how is amount of such rebate calculated. *[B.Com., Punjab & Delhi]*
5. Define the following as per Income-tax Act:
   (*i*) Salaries; (*ii*) Perquisites; (*iii*) Profit in lieu of salary.
6. Describe the methods of savings available to save tax for salaried individual who wants to make a provision for his old age. *[B.Com. Punjab]*
7. Write a detailed note on rebate of tax under section 88 of the Income tax Act, 1961 ? *[Company Secretary Inter June 1992]*
8. Define profits in lieu of salary. To what extent are these exempted from tax ?
9. Write notes on:
   (*i*) Profits in lieu of salary; (*ii*) Qualifying amount; (*iii*) Unrecognised provident fund; (*iv*) Standard deduction; (*v*) Annual accretion; (*vi*) Transferred balance of URPF; (*vii*) House Rent Allowance; (*viii*) Entertainment Allowance; (*ix*) Commutation of pension; (*x*) Leave encashment; (*xi*) Fair Rental Value.

INCOME-TAX (EIGHTH AMDT.) RULES, 1995

Notification No. 9807 — *Dated 7-7-1995*

In exercise of powers conferred by section 295 of the Income-tax Act, 1961 (43 of 1961), the Central Board of Direct Taxes hereby makes the following rules further to amend Income-tax Rules, 1962, namely :

1. (*i*) These rules may be called the Income-tax (Eighth Amendment) Rules, 1995.
   (*ii*) They shall come into force with effect from the 1st day of July, 1995.
2. In the Income-tax Rules, 1962,
   (*a*) After rule 2BA, the following rule shall be inserted, namely :

Prescribed allowances for the purpose of clause (14) of section 10

2BB. (*i*) For the purposes of sub-clause (*i*) of clause (14) of section, 10, prescribed allowances, by whatever name called, shall be the following, namely :

(*a*) any allowance granted to meet the cost of travel on tour or on transfer;

(*b*) any allowance, whether granted on tour or for the period of journey in connection with transfer, to meet the ordinary daily charges incurred by an employee on account of absence from his normal palce of duty;

(*c*) any allowance granted to meet the expenditure incurred on conveyance in performance of the duties of an office or employment of profit;

Provided that free conveyance is not provided by the employer;

(*d*) any allowance granted to meet the expenditure incurred on a helper where such helper is engaged for the performance of duties of an officer or employment of profit;

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(*e*) any allowance granted for encouraging the academic research and training pursuits in educational and research institutions;

(*f*) any allowance granted to meet the expenditure incurred on the purchase or maintenance of uniform for wear during the performance of the duties of an officer or employment of profit.

Explanation—For the purpose of clause (*a*), "allowance granted to meet the cost of travel on transfer" includes any sum paid in connection with transfer, packing and transportation of personal effects on such transfer.

(*ii*) For the purposes of sub-clause (*ii*) of clause (14) of section 10, the prescribed allowances, by whatever name called, and the extent thereof shall be following, namely :

Serial Number	*Name of allowance*	*Place at which allowance is exempt*	*Extent to which allowance exempt*
(1)	(2)	(3)	(4)
1.	Any Special Compensatory Allowance in the nature of Composite Hill Compensatory Allowance or High Altitude Allowance or Uncongenial Climate Allowance or Snow Bound Area Allowance or Avalanche Allowance	I. (*a*) Manipur Mollan/RH-2365 (*b*) Arunachal Pradesh (*i*) Kameng (*ii*) North Eastern Arunachal Pradesh where heights are 9,000 ft. and above (*iii*) Area east or west of Siang and Subansiri sectors. (*c*) Sikkim (*i*) Area North-NE-East of line Chhaten LR 0105, Launchung LR 1902, pt. 4326 LW 1790, pt. 4349 LW 1479, pt. 3601 LW 1471 to mile 13 LW 1367 to Berluk LW 2253 (*ii*) All other areas at 9,000 ft. and above (*d*) Uttar Pradesh Areas of Harsil, Mana and Malari Sub-divisions and other areas of heights at 9,000 ft. and above.	Rupees 600 per month

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(1)	(2)	(3)	(4)
		(e) Himachal Pradesh (i) All areas at 9,000 ft. and above ahead of line joining Puhkaja-kunzomla towards the bower. (ii) Area ahead of line joining Karchham and Shigrila towards the bower. (iii) All areas in Kalpa, Spirit Lahul and Tisa. (f) Jammu and Kashmir (i) All areas from NR 396950 to NR 350850, NR 370790, NR 311776 North of Shaikhra Village, North of Pindi Village to NR 240800. (ii) Areas of Doda, Sank and other posts located in areas at a height of 9,000 ft. and above. (iii) North of line Kud-Dudu and Basttgarh, Bilwar, Batote and Patnitop. (iv) All areas ahead of Zojila served by Road Srinagar-Zojila-Leh in Leh District. (v) Gulmark—All areas forward of line joining Anita Linyan 3309 - Kaunrali 2407 (vi) Uri South - All areas forward of Kaunrali-Kandi 1810 Kustam 1505 Sebasantra 1006 Changez 0507-Jak 19904 Keekar 9704 Jamun 9607 Neeta 0608 (vii) BAAZ Kalyan Bowl - All areas forward of Dulurja 9712-BAAZ 0317 - Shamsher 0416 including New Shamsher 0615 - Zorawar 1017 - Malaugan Base 1027 - Radha 0836 to Nastachun Pass 9847. (viii) Tanghar - All areas west of Nastachun Pass Tangdhar Bowl and on Shamshabari Range and forward of it.	

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		(*ix*) Karan and Machhal sub-sectors- All areas along the line Pharkiangali 0869 to Z Gali 4376 and forward to Shamshabari Range.	
		(*x*) Panzgam, Trehgam and Drugmul.	
	II.	Siachen area of Jammu and Kashmir	Rupees 1200 per month
	III.	All places located at a height of 1,000 metres or more above the sea level, other than places specified at (*i*) and (*ii*) above.	Rupees 150 per month
2. Any Special Compensatory Allowance in the nature of border area allowance or remote area allowance or difficult area allowance or disturbed area allowance	I.	(*a*) Little Andaman, Nicobar and Narcondum Islands	Rupees 650 per month
		(*b*) North and Middle Andamans.	
		(*c*) Throughout Lakshadweep and Minicoy Islands	
		(*d*) All places on or north of the following demarcation line; Point 14600 (2881) to Sala MS 2686 Matau MS 2686 Matau MS 6777 - Sakong MT 1379 2803-Nyapin MO 7525 - River KHRU to its junction with the river Kamla MP - 2226 - Taliha - Yapuik MK 7410 - Gshong MK 9749 - Yinki Yong NF 4324 - Damoroh MF 6208 - Ahinkolin NF 8811 - Kronli MG 2407 - Hanli NM 4096 - Guongon NM 4592 - Loon NM 7579 - Mayuliang NM 0169 - Chawah NM 9943 Kamphu NM 1125 - Point 6490 (NM 1493) Vijaynagar NSA - 486.	
		(*e*) Following areas in Himachal Pradesh :	
		(*i*) Pangi Sub-Division of Chamba District;	
		(*ii*) Baramaur Tehsil of Chamba District;	

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(1)	(2)	(3)	(4)
		(*iii*) Lahul and Spiti District (*iv*) Kinnaur District; (*v*) Dodra-Kawar area of Rohru Tehsil, Parganas of Pandrabis and Atharabis, Gram Panchayats of Munish, Derkaili and Kashapat of Rampur Tehsil of Simla District; (*vi*) Pargana of Pandrabis of Kulu District; (*vii*) Chhota Bhangal and Bara Bhangal area of Palampur Sub-division of Kangra District; (*viii*) Gram Panchayat Deothi (Teklech area) and Parganas of Chhaibis, Naubis, Sarahan and Barabis of Rampur Tehsil of Simla District; (*ix*) Chhuhar Valley of Joginder nagar Tehsil of Mandi District; (*x*) Mangal Panchayat area of Solan district; (*xi*) Cuter - Seraj and Malana Panchayat area of Kulu District; (*xii*) Janardru Panchayat area of Bhatiyat Tehsil of Chamba District; (*xiii*) Mahog Sarhan, Gopalpur, Teban, Pelhi, Nanj, Khanoj, Bagra, Saiaj Mahundi and Balidhar Panchayat of Karseg Tehsil; (*xiv*) Transgiri Tract of Simur District; (*xv*) Simla Town and its suburbs (Mashobra, Dhali, Taradevi, Kasumppti, Jatog and Tulu).	
		(*f*) Chimptuipui District of Mizoram and areas beyond 25 km. from Lungali town in Lungali District of Mizoram.	

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(*g*) Following areas in Jammu and Kashmir :

(*i*) Niabat Bani, Lohi, Malahar and Macchodi in Kathua District;

(*ii*) Dudu Basantgarh, Llander Thamg Illaqa;

(*iii*) All areas in Tehsil Mahore except those specified at III(g)(*i*) below in Udhampur District;

(*iv*) Illaqas of Padder in Kishtwar Tehsil and Niabat Nowgam in Kishtwar of Doda District;

(*v*) Noyama, Zansar and Nobre of Leh District;

(*vi*) Entire Gurez-Niabat, Tangdhar Sub-Division and Keran Illaqa of Baramulla District.

(*h*) Following areas of Uttar Pradesh :

(*i*) Dharachula;

(*ii*) Munsiyari;

(*iii*) Joshimath; and

(*iv*) Bhatwari Development Blocks (except District headquarters of

(II) Installations in the Continental Shelf of India and the Exclusive Economic Zone of India. — Rupees 1100 per month

(III) (*a*) Throughout Arunachal Pradesh other than areas covered by those specified at 1 (*d*) above. — Rupees 525 per month

(*b*) Throughout Nagaland.

(*c*) Throughout Sikkim.

(*d*) South Andaman (including Port Blair)

(*e*) Throughout Lunglei District) (excluding areas beyond 25 km. from Lunglei town) of Mizoram.

(*f*) Dharmanagar, Kailasahar, Amarpur and Khowai in Tripura.

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(1)	(2)	(3)	(4)
		(*g*) Following areas in Jammu and Kashmir : (*i*) Areas up to Goel from Kamban side and areas up to Arnas from Keasi side in Tehsil Mahore of Udhampur District; (*ii*) All places in Leh District other than those specified at I(*g*) above; (*iii*) Matchill in Baramulla District.	
	(IV)	(*a*) Throughout Aizawl District of Mizoram	Rupees 375 per month
		(*b*) Throughout Tripura except areas those specified at III (*i*) above.	
		(*c*) Throughout of Manipur.	
		(*d*) Following areas of Himachal Pradesh; (*i*) Janjehli Block of Chachlet Tehsil of Mandi District; (*ii*) Chopal Tehsil of Shimla District; (*iii*) Transgiri Tract of Sirmaur District; (*iv*) Churah Tehsil of Chamba District; (*v*) Kunr Panchayat and Balaj Parghana of Chamba Tehsil of Chamba District; (*vi*) Dalhousie town; (*vii*) Janjheli Block of Chachlet Tehsil in Mandi District; (*viii*) Trah chopal Tehsil of Shimla District; (*ix*) Churah Tehsil of Chamba District; (*x*) Munr Panchayat and Balaj Pargana of Chamba Distt; (*xi*) Karsog Tehsil; (*xii*) Rampur Tehsil;	
		(*e*) Following ares in Jammu and Kashmir Areas in Poonch and	

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		Rajouri Districts excluding the towns of Poonch and Rajouri and Sunderbani and urban areas in the two Districts.	
		(*f*) Following areas in Jammu and Kashmir : Areas not included in I(*g*), III(*g*) and (IV)(*e*) above but which are within the distance of 8 km. from the line of actual control or at places which may be declared as qualifying for border allowance from time to time by the State government for their own staff.	
		(*g*) Following areas in Uttar Pradesh : Areas other than those covered in the border district of Uttar Kashi, Chamoli and Pithoragarh, including District Headquarters of Uttarkashi, but excluding Champavat Tehsil of Pithoragarh District.	
		(V) Jog Falls in Shimoga District in Karnataka	Rs. 300 per month
		(VI) (*a*) Manali-Ujhi area, Parvati and Lagg Valley and Banjar Blocks of Kulu District in Himachal Pradesh.	Rupees 100 per month
		(*b*) Throughout Assam and Meghalaya	
3.	Tribal Area Allowance	(*a*) Madhya Pradesh (*b*) Tamil Nadu (*c*) Uttar Pradesh (*d*) Karnataka (*e*) Tripura (*f*) Assam (*g*) West Bengal (*h*) Bihar (*i*) Orissa	Rupees 100 per month
4.	Any allowance granted to an employee working in any transport system to meet his personal expenditure during his duty performed in	Whole of India	70 per cent of such allowance upto a maximum of Rupees 3,000 per month

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(1)	(2)	(3)	(4)
	the course of running of such transport from one place to another place, provided that such employee is not in receipt of daily allowance		
5.	Children Education Allwoance	Whole of India	Rupees 50 per month per child upto maximum of two children
6.	Any allwoance granted to an employee to meet the hostel expenditure of his child	Whole of India	Rupees 150 per month per child upto a maximum of two children
7.	Compensatory Field Area Allowance	(*a*) Following Areas in Arunachal Pradesh : (*i*) Tirap and Changlang districts; (*ii*) all areas north of line joining point 4448 in LZ 4179 - Nukme Dong MS 3272 - Sepla MT 2969 - Plain MO 9213 - Daporijo NR 5841- Along NL 1273- Hunli NM 3196 - Tidding Tuwi MT 6369 - Hayuliang NN 0170 - Tawaken MT 8136 - Champai Bun NM 8814, all inclusive; (*b*) Throughout Manipur and Nagaland; (*c*) Following areas in Sikkim : All areas north and north east of line joining Phalut LV 4750 - Gezing LV 7059 - Mangkha LV 6160 - Penlang La LW 0666 - Rangli LW 1448 - BP 1 in LW 2453 on Indo-Bhutan Border, all inclusive.	Rupees 975 per month

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(*d*) Following areas in Himachal Pradesh :
All areas east of line joining Umasila NV 3951 - Udaipur NY 8663 - Manikaran SB 2300 - Pir Parbati Pass TA 1459 - Taranda TA 2335 - Barasua - Pass TA 8801, all inclusive.

(*e*) Following areas in Uttar Pradesh :
All areas north and north-east of line joining Barasua Pass Gangnani TG 1362 - Govind Ghat TG 0937 - Tapovan TH 1822 - Musiari TN 8982 - Relagad TO 2466, all inclusive.

(*f*) Following areas in Jammu and Kashmir :

(*i*) areas north and east of line joining Zojila MU 3036 - Baralachala NE 6672 along the Great Himalayan Range, all inclusive;

(*ii*) all areas west of line joining Point 1556 in NR 5470 - Gulmarg MT 3105 - Naushara MY 3105 - Ringapat MT 2133 - Handwara MT 2043 - Laingyal MT 2339 - Point 8405 in NG 4565 - north of line joining Point 8403 - Bunakut MT 5453 - Razan NN 2239 - Zojila, all inclusive.

(*iii*) all areas west of joining tip of Chicken Neck RD 7073 - Canal junction RD 6364 - Mawa Brahmana RD 6183 - Chauki RD 6393 - Raod Junction RD 6499 - Baramgala MY 3854 - Point 1556 in NR 5470, all inclusive.

8. Compensatory Modified Field Area Allowance

(*a*) Following areas in Punjab and Rajasthan :
areas west of line joining Jessai, Barmer,

Rs. 375 per month

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(1)	(2)	(3)	(4)
		Jaisalmer, Pokharan, Udasar, Mahajan Ranges, Suratgarh, Lalgarh, Jattan, Abohar, Govindgarh, Fazilka, Jadiala Guru, Moga, Dholewal, Deas, Bir Sarangwal, Hussainiwala, Dera Baba Nanak, Laisain Pulge upto the international border, all inclusive; (*b*) Following areas in Haryana, — Satrod (Hissar). (*c*) Following areas in Himachal Pradesh : areas north of line joining Narkhanda, Keylong upto Field Area line/High Altitude line. (*d*) Following areas in Arunachal Pradesh and Assam : (*i*) Cachar and North Cachar districts of Assam including Silchar; (*ii*) all areas of Arunachal Pradesh and Assam north of river Brahmaputra except Tejpur, Misamari and Field Areas; (*e*) Throughout Mizoram and Tripura; (*f*) Following areas in Sikkim and West Bengal : areas northwards of line joining Sevoke LV 9112-Burdong LV 985 (Sherwani LV 9453-Bagrakot LW 0113 - Damdim LW 1109 - New Mal-Hasimara-QB 7894 Ganga Ram Tea Estate QA 1377 upto the High altitude line/Field Area line/ International border, all inclusive. (*g*) Following areas in Uttar Pradesh : areas north of line joining Uttarkashi, Karan Prayag,	

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		Gauchar, Joshimath, Chamoli Rudra Prayag, Askote, Charamgad, Dharchula, Kausani and Narendra Nagar upto international border, all inclusive.	
		(*h*) Following areas in Jammu and Kashmir :	
		(*i*) areas west of line joining Pattan, Baramula, Kupwara, Drugmula, Panges, Mankes, Buniyar, Pantha Chowk, Khanabal, Anantnag, Khundru and Khru upto the existing High Altitude line, all inclusive;	
		(*ii*) areas west of line joining; BP - 19, Brahmana-di-Bari, Jindra, Dhansal, Katra, Sanjhi Chatt, Batote, Patni Top, Ramban and Banihal upto the existing High altitude line, all inclusive.	
9.	Any special allowance in the nature of counter-insurgency allowance granted to the members of armed forces operating in areas away from their permanent locations for a period of more than 30 days.	Whole of India	Rs. 975 per month

Provided that any assessee claiming exemption in respect of the allowances mentioned at serial numbers 7 and 8 shall not be entitled to the exemption in respect of the allowance referred to at serial number 2:

Provided further that any assessee claiming exemption in respect of the allowance mentioned at serial number 9 shall not be entitled to the exemption in respect of disturbed area allowance referred to at serial number 2:

[F. No. 142/9/95 - TPL]

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2 INCOME FROM HOUSE PROPERTY

Definition of head—explanation of the terms used—Exempted incomes from house property—Annual Value—determination of annual value—Let out—self-occupied—Deductions out of annual value—Chart—Illustrations—Questions.

DEFINITION OF THE HEAD (Section 22)

The income from houses, buildings, bungalows, godowns etc. is to be computed and assessed to tax under the head "Income from house property". The income under this head is not based upon the actual income from the property but upon notional income or the annual value of that building.

Section 22 of the Income-tax Act says:

The annual value of property consisting of any building or lands *appurtenant* thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head 'Income from house property'.

For income to be taxed as 'Income from house property' the following points should be noted carefully:

1. Building or Land Appurtenant thereto. The scope of this head of income is limited to the income from buildings or lands appurtenant (attached or situated in the vicinity of building) to buildings only. Buildings include residential houses, bungalows, docks, warehouses, any block of bricks or stone work covered by a roof etc. Land which is not appurtenant to any buildings does not come within the scope of this section.

2. Annual Value. The meaning of word 'Annual value' is very significant because the annual value of the building or land appurtenant thereto is to be taxed and not the rent received. The annual value is to be determined according to the provisions of section 23 of Income-tax Act. These are discussed later in this chapter.

3. The Assessee should be the owner of the property. It is only the owner of the house property who can be taxed under this head of income. The tax under this section is in respect of the legal or beneficial owner and not the occupation or possession of house property'. Therefore, income from subletting, will be chargeable under head 'Income from other sources' and not under house property'. So only the

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owner, may be legal or deemed owner, is liable to tax under this head of income, unless the house property is used by him for the purposes of his own business or profession. The question of ownership may be noted in the following cases:

(*i*) If the land was taken on lease (long time) and a super-structure constructed, the person who takes land on lease will be treated as its owner.

(*ii*) Where the property is mortgaged, it is the mortgager alone and not the mortgagee who can be treated as the owner.

(*iii*) Where the property was constructed in the name of partnership, it is the firm which is assessable as owner and not the individual partners.

(*iv*) A person whose property is vested in the Custodian of Evacuee Property is not the 'owner' thereof for the purposes of this section.

(*v*) Where the assessee takes a building on lease and he is deriving some income by subletting or re-letting, this income will be taxable under the head 'Income from other sources' and not under the head 'Income from house property'.

(*vi*) In case houses were constructed by a cooperative building society and allotted or leased out to its members, the member shall be deemed to be the owner of the buildings or part thereof as the case may be.

In one of the cases, Supreme Court decided that the owner must be a person who can exercise the rights of the owner, not on behalf of the owner but as his own right.

Deemed Owner of House Property

According to Section 27 of Income-tax Act the assessee in following cases is deemed to be the owner of the house property, though not owner of the house property:

(*i*) As individual who transfers otherwise than for adequate consideration any house property to his or her spouse, not being a transfer in connection with an agreement to live apart or to a minor child not being a married daughter, shall be deemed to the owner of the house property so transferred.

(*ii*) The holder of an impartible estate shall be deemed to be the individual owner of all the properties comprised in the estate.

(*iii*) A member of a co-operative society to whom a building or part thereof is allotted or leased under a house building scheme of the society, shall be deemed to be the owner of that building or part thereof.

4. It is not used for purposes of assessee's business or profession. Where the assessee is carrying on business or profession in his own house, building or in a portion of it and the income of such business or profession, is taxable under the head 'Profits or gains of business or profession', the annual value in respect of property or portion of it is not taxable under this head of income. As the business is being carried on in the assessee's own premises, so no rent will be allowed as expenditure to the assessee in respect of these premises.

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But where the profits of such business or profession are not chargeable to tax, the annual value of the (owned) premises shall be computed and charged under the head 'house property'.

5. Quarters let to Employees of Assessee's own Business. In case a portion of the business premises is let out to employee or employees of the business for residence and this letting out is incidental or is essential for the efficient running of the business of the assessee, the rent received from such employee or employees will not be taxable as income from house property'. Similarly, if the assessee constructs residential houses and lets out to such employees of his business whose stay there is essential or incidental to the efficient and proper conduct of his business, the rental income from such quarters would be outside the purview of this source of income and it will be considered as business income. If stay of the employee is not essential to assessee's business, any rent received from them shall be assessee's income from house property.

6. Dispute about ownership. It is the owner who is liable to pay tax on the income of the house property and in case of a dispute about ownership the person who receives rent shall be liable to pay tax till the dispute about ownership is settled.

7. Letting out of Building along with furniture etc. Rent received from letting out of building alongwith the furniture etc. shall be split out in two parts, *i.e.*, (*i*) from building, and (*ii*) rent from furniture, other amenities. Rent received from the first category only is assessable under this head of 'income' and the rent received from second part is liable under the head 'income from other sources'. Where such rent cannot be split up like this, the whole rent received shall be taxable under the head 'income from other sources' and not under house property.

EXEMPTED HOUSE PROPERTY INCOMES

Under section 10 of the Income-tax Act 1961 following incomes from house property are exempted from tax. These incomes are not to be included in the total income of assessee. Hence no tax is payable on such incomes. These incomes are:

1. Agricultural House Property [Section 21(1)(c)]. Income from such house property which is situated on or in the immediate vicinity of agricultural land which is used for agricultural purposes by cultivator is exempted from tax.

2. House property held for charitable purposes [Section 11]. Any income from a house property held for charitable or religious purposes *e.g.*, rent from shops owned by a temple is also exempted.

3. Self-occupied but vacant house [Section 23(3)]. In case an assessee keeps one of his own houses reserved for self-occupation but is living in a rented house elsewhere due to his employment or profession the income from such house is taken to be nil.

4. House used for own business or profession. There is no income chargeable to tax under this head from such house property.

5. Property held by resistered trade union [Section 10(24)]. Income from a house property owned by a resistered trade union is not to be included in its G.T.I.

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6. Letting of godowns etc. [Section 10(29)]. In case of an authority constituted under any law for the time being in force for the marketing of commodities, and income derived from the letting of godowns or warehouses for storage or facilitating the marketing of commodities is fully exempted.

In case of a Cooperative Society

Income from following house properties is includible in Gross Total Income but a deduction is allowed from the Gross Total Income.

1. Income from any other Property [Section 80P(2)(b)]

In case the gross total income of a co-operative society does not exceed Rs. 20,000, any income derived by it from house property and included in its gross total income, the whole of such income is allowed as deduction while computing its total income. Co-operative society in this case should not be a housing society or an urban consumer's co-operative society or a society carrying a transport business.

2. Letting out of godown by co-operative societies [Section 80P(2)(c)].

If a co-operative society lets out godowns or warehouses for storage, processing or facilitating the marketing of commodities, the whole of its income derived from letting out of houses or storages etc. is deductible in computing its total income.

ANNUAL VALUE (Section 23)

Tax is levied on the 'annual value' of house property. The whole topic of 'Income from House property' revolves around 'annual value' of the property. As such it is very important to understand the meaning of word 'annual value'.

Section 23(1) of Income-tax Act has defined the word 'annual value', as "the sum for which the property might reasonably be expected to let from year to year". The annual value is the value which any house can fetch from the market under the prevailing circumstances such as local conditions, the demand for house, municipal valuation, type and standard of construction, rent for similar type of house in the similar type of locality, etc. From the explanation it should be clearly understood that the annual value does not mean the rent derived or rental value of the house but the notional rent at which the house can reasonably be let out. A property can be let out at a rent which is lower than its reasonable rent but it annual value will be its reasonable rent.

The Taxation Laws (Amendment) Act, 1975 has changed the term *Annual value* as under:

The annual value of any property shall be deemed to be—

(*a*) the sum for which the property might reasonably be expected to let from year to year; or

(*b*) where the property is let and the annual rent received or receivable by the owner in respect thereof is in excess of the sum referred to in clause (*a*), the amount so received or receivable.

In case standard rent is fixed under Rent Control Act of any State the annual value of a let out house shall be:

(*i*) Standard Rent fixed under Rent Control Act; or

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(*ii*) Actual rent received; whichever is higher.

[Mrs. Sheela Kaushik vs. C.I.T. (1981) Supreme Court]

Meaning of Annual Rent [Section 23(1) Explanation (1)]

1. Annual Rent means the actual rent received or receivable by the owner if property is let out throughout during the year.
2. In case property is let out for a part of the year (due to vacancy) the annual rent shall be the amount which bears the same proportion to the amount of actual rent received for the period which the property is let, as the period of 12 months bears to it. It means actual rent received shall proportionately increase.

Illustration 1. Calculate the annual rent of a house which was let out @ Rs. 900 p.m. from 1.4.96 to 31.8.96 and @ Rs. 1,200 p.m. from 1.11.96 to 31.3.97. It was vacant from 1.9.96 to 31.10.96.

Solution

Calculation of Annual Rent	Rs.
Actual Rent for 5 months @ Rs. 900 p.m. (1.4.96 to 31.8.96)	4,500
Actual Rent for 5 months @ Rs. 1,200 p.m. (1.11.96 to 31.3.97)	6,000
Actual Rent for 10 months	10,500

This rent will be raised proportionately to 12 months (Rs. 10,500 × 12/10) = Rs. 12,600.

Q. No. 1

Calculate the annual rent of a house for the previous year 1996-97 which was letout from 1.4.96 @ Rs. 3,000 p.m. and from 1.10.96 @ Rs. 4,000 p.m. During the period 1.8.96 to 30.9.96 it was vacant.

[Hints: Annual Rental Value Rs. 43,200]

3. For the purposes of calculation of Annual value, the term annual rent means:
   (*i*) Rent actually received from the tenant;
   (*ii*) Deduct the cost of facilities or amenities provided by the owner to tenant out of rent received and balance is taken as *'annual rent'*.

The facilities provided by owner can be:

(*i*) Lift or pump maintenance; (*ii*) Lighting of common stairs; (*iii*) Swimming pool or garden maintenance expenses; (*iv*) Salary of gardener or watchman; (*v*) Water & electricity charges if included in rent.

The comparison with Fair Rent etc. is to be made after deducting these expenses.

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Illustration 2. Mr. X has constructed a multistorey building at Delhi consisting of 40 flats. Each flat is let out @ 1,000 p.m. The municipal authorities have fixed the rental value of this property as Rs. 4,50,000 p.a. The owner bears the following expenses:

		Rs.
(*i*)	Lift maintenance	12,000 p.a.
(*ii*)	Pump maintenance	8,000 p.a.
(*iii*)	Salary of Gardener and Watchman	3,600 p.a.
(*iv*)	Swimming pool expenses	9,000 p.a.

Compute the Annual Rental Value for the property.

Solution

Computation of Annual Rental Value

			Rs.
Municipal Rental Value			4,50,000
or			
Annual Rent *i.e.*	Rs.	Rs.	
Actual Rent (40 × 1,000 × 12)		4,80,000	
Less: (*i*) Lift maintenance	12,000		
(*ii*) Pump maintenance	8,000		
(*iii*) Salary of Gardener and Watchman	3,600		
(*iv*) Swimming pool exp.	9,000		
		32,600	
			4,47,400

Whichever is higher is ARV *i.e.*

Municipal Rental Value of Rs. 4,50,000 shall be taken as ARV.

Q. No. 2.

Compute Annual Rental Value in following case:

(*i*)	Municipal Rental Value	Rs. 48,000 p.a.
(*ii*)	Actual Rent received	Rs. 50,000 p.a
(*iii*)	Lift and pump maintenance charges paid by owner	Rs. 6,000 p.a.
(*iv*)	Salary of common Gardener and Watchman contributed by tenants Rs. 4,800 p.a.	

[Hints: ARV is Rs. 48,000]

Determination of Annual value in case of different types of house properties

The house properties are divided into following categories for the purposes of determining annual value:

1. Let-out houses.
2. Newly built let-out residential house completed after 31.3.1970 but before 1.4.1992.
3. Self-occupied houses. (Nil)

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4. Deemed to be let-out houses.
5. The houses not in rentable form.
6. The house which could not be occupied by the owner due to employment or business reasons or due to reasons beyond his control.
7. Own business set-up in own house property.
8. In case of co-owners.

1. Let-out houses. In case the house property is let out to a tenant, there can be two types of amounts, *i.e.*, (i) the rent received, and (ii) the municipal valuation or reasonable value of the house property. As explained earlier, the annual value is the value at which the house can reasonably be let out, so the greater of the above two sums is taken to be the reasonable rent the house can fetch. So this value can be termed as "Annual Rental Value".

The municipal taxes or any tax levied by the local authority in respect of the relevant house property (including service taxes like fire tax, water tax, educational cess etc.) borne by the landlord, are allowed to be deducted from the Annual Rental Value and the amount so calculated will be annual value in the case of let-out house. These are allowed only if actually paid by the landlord during the year.

Illustration 3. Mr. Ashok is the owner of a house which is let-out at a rent of Rs. 500 p.m. The municipal taxes are equal to 10% of the rent received.

Compute the annual value of the house, if

(*i*) The municipal taxes are paid by Mr. Ashok, and

(*ii*) 1/2 of the municipal taxes are borne by the tenant.

Solution

		Rs.
(*i*)	Annual Rental value [@ Rs. 500 p.m.]	6,000
	Less: Municipal Taxes @ 10% of rent received	600
	Annual value	5,400
(*ii*)	Annual Rental value @ Rs. 500 p.m.	6,000
	Less: Municipal Taxes 50%	300
	Annual value	5,700

Q. No. 3

Compute Annual value if—actual rent of a house is Rs. 24,000 p.a.; its fair rental value is Rs. 25,000 p.a. and its municipal rental value is Rs. 27,000 p.a.

Local taxes charged by municipal committee are @ 10% of MRV and charged in two instalments every year. The owner paid one instalment due on 30.6.96 but could not pay the second instalment due on 31.12.96.

[Hints: Annual value Rs. 25,650]

The important point to be noted is that the deduction will be allowed in case of those municipal levies only which are borne by the landlord or the owner of the

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house property, *i.e.*, if any part of municipal or local taxes are met or paid by the tenant, the same shall not be allowed to be deducted while calculating net annual value.

2. Newly built let-out residential houses—Deduction of New Construction Allowance

Residential Houses, the construction of which started after 1st April 1961 and completed after 31st March 1982, but before 1st April 1992. For the residential houses of course for letting out purposes, the construction of which started after 1st April 1961 and completed after 31st March 1982 but upto 31.3.92, a deduction @ Rs. 3,600 p.a. per unit or Gross Annual Value for relevent period whichever is less is allowed for a period of 5 years from date of completion of construction of house.

No New Construction Allowance is to be allowed for houses completed after 31.3.92

Example. *Residential unit completed on 1.7.91 (for assessment year 1997-98)*

	Rental Value @ Rs. 500 p.m.	6,000
Less:	Municipal Taxes	600
	Gross Annual Value	5,400
Less:	New Construction Allowance for 3 months	900
	or Gr. A.V. Rs. 5,400 $\times \frac{3}{12}$ = 1350) w.e. is less	
	Net Annual Value	4,500

Conditions for claim of New Construction Allowance

1. House property must be let out;
2. It may be let out for rent or given without rent;
3. It must be residential house property but may be used for non- residential purposes; *[J.V. Desai v C.I.T. (AP)]*
4. Construction of such house property must have started after 1.4.61;
5. Construction of such house property must have been completed between 1.4.82 to 31.3.92.
6. The deduction is allowed for a period of 5 years from date of completion. After which this benefit is withdrawn.
7. It is allowed for all units in a house property. Unit means a unit having a separate kitchen, or a water meter or electricity meter or a municipal allotted separate number.

Illustration 4. Mr. A owns a house. The construction of this house was started in 1987 but completed on 31st December 1991 and let out on 1st January 1992. The rental value is Rs. 3,600 p.a. and Municipal Taxes are 10% of rental value. Compute the annual value of this house property for the previous years during which *he is entiiled to new construction allowance.*

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Solution

	Rs.
Previous Year: 1991-92	
Rental value for 3 months (*i.e.*, January '92 to March '92)	900
Less: Municipal Taxes	90
Gross Annual Value	810
Less: New Construction allowance for 3 months $\left(3{,}600 \times \frac{3}{12}\right)$ Rs. 900 or Gr. A.V. w.e. is less	810
Net or adjusted Annual Value	Nil
For previous years 1992-93 to 1995-96 every year the annual value will be:	
Rental Value for full year	3,600
Less: Municipal Taxes	360
Gross Annual Value	3,240
Less: New Construction allowance for full year or gross annual value, w.e. is less	3,240
Net Annual Value	Nil
Previous Year: 1996-97	
Rental Value for 9 months	2,700
Municipal Taxes	270
Gross Annual Value	2,430
Less: New Construction allowance for 9 months Rs. 2,700 but restricted to annual value for that period	2,430
Net Annual Value	Nil
Rental Value for 3 months	900
Less: Municipal Taxes	90
Net Annual Value	810

It can be solved in the following manner also :

	Rs.
Rental value for full year	3,600
Less: Municipal Taxes	360
Gross A.V.	3,240

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Less : New Construction Allowance for 9 months
(3,600 × 9/12 = 2,700) or
Gross A.V. for 9 months (3,240 × 9/12) Rs. 2,430
which ever is less 2,430

Net A.V. 810

Q. No. 4

Compute the net annual value for the previous year ending on 31.3.1997 for each case separately:

Particulars	A	B	C
	Rs.	Rs.	Rs.
MRV	6,000 p.a.	3,600 p.a.	24,000 p.a.
Actual Rent	7,200 p.a	3,000 p.a.	20,000 p.a.
Standard Rent	—	—	21,000 p.a.
Date of completion	1.9.96	31.10.91	1.10.91
Municipal Taxes	10% of MRV	Rs. 360 p.a.	Rs. 2,400 p.a.

All the three houses are residential house properties.

[**Hints:** Net annual value A Rs. 3,850; B Rs. 1,350; C Rs. 16,800]

3. **Self-occupied House [Section 23(2)].** Self-occupied house is that house in which the owner resides himself or where the house property is in the occupation of the owner for the purposes of his own residence.

The Finance Act, 1986 gave a substantial relief to the owners of self-occupied houses. The recommendation given by Chaukasi Committee has been implemented. The effect of this amendment is that the house in which assessee is living himself, is now exempted from tax. The Net Annual Value of such house is taken to be Nil. The amended provisions of section 23(2) are as under:

A—Only One House Under Self-Occupation for Full Year

A house or part of a house in the occupation of the owner for the purposes of his own residence—which is not actually let during any part of the previous year and no other benefit therefrom is derived by the owner the annual value of such house or part of the house shall be taken to be nil. [Section 23(2)(a)(i)]

B—Only one House—Part of the Year Self-Occupied and Part of the Year Let-Out or partly Let-Out and partly self occupied

In case a house is let during any part or parts of the previous year, that part of the annual value (annual value being determined in the same manner as if the property had been let) which is proportionate to the period during which the property is in the occupation of the owner for the purposes of his own residence, or, as the case may be, where such property is let out in parts, that portion of the annual value appropriate to any part which was occupied by the owner for his own residence, which is proportionate to the period during which such part is wholly occupied by him for his own residence shall be deducted in determining the annual value.

[Section 23(2)(a)(ii)]

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The deduction under this sub-clause shall be made irrespective of whether the period during which the property or, as the case may be, part of the property was used for the residence of the owner precedes or follows the period during which it is let.

Restriction on deductions u/s 24—When net annual value of house (as mentioned above) is reduced, the balance net annual value of let-out period shall be eligible for deductions u/s 24. The expenses for full year shall be eligible for deduction. The total of all deductions in this case cannot exceed the balance net annual value. In case such total is more than balance net A.V., it shall be restricted to such amount of balance net. A.V. and excess if any shall be ignored. [Proviso to Section 24(2)] [*See Illustration No. 14*].

Illustration 5. Compute the net annual value (for each case separately) from particulars given below:

Municipal Rental value	Rs. 30,000 p.a.
Fair Rental value	Rs. 36,000 p.a.
Municipal Taxes	10% of MRV
Date of Completion 1.7.91	

Case I : Self occupied for whole year

Case II : Let out from 1.4.96 to 31.7.96 and self occupied from 1.8.96 onwards

Case III : Half is self occupied for whole year and half is let out from 1.4.96 to 31.10.96 and self occupied from 1.11.96 onwards.

Case IV : Half is used for own business for whole year and $^1/_2$ is let out from 1.4.96 to 31.5.96 and self occupied from 1.6.96 onwards.

Solution

Computation of Annual value

Case I : *Self occupied for whole year*

	Rs.
Municipal Rental value	30,000
Fair Rental value	36,000
whichever is higher is ARV	36,000
Deduct Municipal Taxes 10% of MRV	3,000
Gross Annual value	33,000
Reducted to NIL u/s 23 (2)	33,000
	Nil

Case II : *Let out for 4 months and self occupied for 8 months*

	Rs.
Municipal Rental value	30,000
Fair Rental value	36,000

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whichever is higher is ARV	36,000
Less : Municipal Taxes 10% of MRV	3,000
Gross A.V.	33,000
Reduced to Nil for 8 months being self occupied u/s 23(2)	22,000
Gross Annual value for let out period	11,000
New Construction Allowance for 3 months ($3,600 \times {}^{3}/_{12}$)	900
Net A.V.	10,100

Case III : 1/2 self occupied for whole year and 1/2 let out for 7 months & self occupied for 5 months

Municipal Rental value	30,000
Fair Rental value	36,000
w.e. is higher is Annual Rental value	36,000
Less : Municipal Taxes	3,000
Gross A.V.	33,000
Less : 1/2 reduced to Nil u/s 23(2)	16,500
	16,500
Less : reduced to Nil u/s 23(2) for 5 months	6,875
Gross A.V. for let out period	9,625
New Construction Allowance for 3 months ($3,600 \times {}^{3}/_{12}$)	900
Net AV	8,725

Case IV : Half used for own Residence/let out

M.R.V. of $^{1}/_{2}$ house	15,000
Fair Rental value of $^{1}/_{2}$ house	18,000
whichever is higher is ARV	18,000
Less : Municipal Taxes $^{1}/_{2}$	1,500
Gross Annual value	16,500
Less : reduced to Nil u/s 23(2) for 10 months	13,750
Gross A.V. for Let out period	2,750
Less : New Construction Allowance for 2 months	600
Net A.V.	2,150

$^{1}/_{2}$ *used for own business*—Annual value is taken as Nil

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Q. No. 5

Compute the Net Annual Value for each case separately from particulars given below:

MRV Rs. 24,000 p.a.

Fair Rental Value Rs. 30,000 p.a.

M. Taxes—10% of M.R.V.

Date of completion 31.12.91

Case I : Self-occupied for whole year

Case II : Let-out from 1.4.96 to 31.7.96 and self-occupied for rest of the year

Case III : 1/2 is self-occupied for whole year; the remaining half is let-out from 1.4.96 to 30.11.96 and self-occupied for rest of the period

Case IV : 1/2 is used for own business remaining half is let-out from 1.4.96 to 31.5.96 and self-occupied from 1.6.96 to 31.3.97.

[**Hints**. *Case I* Nil; *Case II* Rs. 8,000; *Case III* Rs. 6,800; *Case IV* Rs. 1,700]

C—More than One House Under Self-occupation

When more than one house is in the occupation of the owner for the purpose of his own residence, the provisions of clause (a) shall apply in respect of one such house, which the assessee may, at his option, specify in this behalf; [Section 23(2)(b)]

D—Treatment of Other Self Occupied Houses

When more than one house or houses are in the occupation of the owner for the purposes of his own residence the annual value of house or houses, other than the house in respect of which the assessee has exercised an option under clause (b), shall be determined under subsection (1) as if such house or houses had been let.

Explanation: "When any such residential unit as is referred to in the second proviso to sub-section (1) is in the occupation of the owner for the purposes of his own residence, nothing contained in that proviso shall apply in computing the annual value of that residential unit".

4. **Deemed to be let-out.** When assessee has more than one house in his own occupation for the purpose of his residence, only one house of his choice is treated as self-occupied house which is exempted from tax and other houses are deemed to be let-out houses. The houses which are occupied by relatives cannot be treated as self-occupied. Such houses are deemed to be let-out houses.

Section 23(2A) deals with adjustments out of annual rental value in case of deemed to be let-out houses. According to it—

For the removal of doubt it is hereby declared that, where the property consists of more than one houses and out of these houses one house is in the occupation of assessee and others are given to friends or relatives without rent, the annual value of the houses, other than that the annual value of which is required to be determined under clause (1) of sub-section (2) shall be applicable in same manner as in case of actually let-out houses.

5. **Annual value in case the house is not in rentable form.** The annual value is the value at which the house can reasonably be let out from year to year. If in any

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case, the house cannot be let out for one reason or the other, the annual value of the house is taken as nil.

But no loss can be returned in this case. Under this case the house remains vacant not due to the fact that the landlord is not interested for its letting out. The following example will clarify this point:

(*i*) Mr. A owns a house at Simla. The house could not be let out for the last 11 years because the site of the house is such that it is 5-6 miles away from Simla at a very lonely place. So, if this house could not be let out, the annual value will, of course, be nil.

(*ii*) Mr. A started the renovation work of his office at Delhi. Due to shortage of cement, he could not complete the work for the last 3 years. So the annual value for 3 years will be nil.

6. **The house could not be occupied by the owner due to employment, business reasons** [Section 23(3)]

With effect from 1.4.86 *i.e.* assessment year 1987-88 following has replaced the above provisions:

Where assessee has only one house under self-occupation and it cannot actually be occupied by him because he is living in a rented house at another place due to his employment, business or profession, the annual value of such house is taken to be NIL provided that—

(*a*) such house is not actually let; and

(*b*) no other benefit is derived by the owner from this house.

This simply means that net Annual value of vacant self-occupied house is taken as NIL if assessee does not derive any benefit from such house during the relevant previous year and he lives in rented house at another place due to his employment, business or profession.

7. **Own business set-up in own house property.** This type of house is not taken as part of house property. So annual value as far as such house property is concerned shall be taken as nil. The house is treated under the head business or profession.

8. **In case of co-ownership.** Under section 26, where a house property is owned jointly and the shares of the co-owners are definite and ascertainable, the share of each partner is assessed on him as part of his total income. Each co-owner's portion is to be treated as a separate house.

DEDUCTIONS [SECTION 24(1)]

Out of the net annual value computed in accordance with the above-mentioned provisions following deductions are allowed. These deductions have been grouped into two parts: (a) For self-occupied house, (b) For let-out house property.

A. For Self-occupied House. In case annual value of self-occupied house is taken as NIL, any interest on loan taken to purchase, construct, repair or renovate the house, interest is allowed as deduction up to actual amount of such interest or

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Rs. 15,000 in a previous year whichever is less. As such it results into loss from this house. This loss can be adjusted from income of any other house or from any other head but cannot be carried forward.

B. For Let-out House Property

1. Repairs and Collection Charges. The Finance Act 1992 has combined the deduction of repairs and collection charges. With effect from assessment year 1993-94 the deduction for repairs and collection charges shall be allowed at the rate of 1/5th of annual value and deduction for collection charges shall not be allowed seperately.

Illustration 6. Mr. R.P. Seth owns a house property of the annual rental value of Rs. 8,000 which he has let out to Mr. Kamthan at Rs. 7,000 p.a. The other expenses of Mr. Seth in connection with house property amount to Rs. 2,500.

You are required to calculate his taxable income from property.

Solution

Computation of house property income of Mr. R.P. Seth

		Rs.
Annual Rental Value		8,000
Less: Municipal Taxes		—
Annual Value		8,000
Deductions:	Rs.	
Repairs & Collection Charges		
1/5th of Rs. 8,000	1,600	
Other expenses	2,500	
		4,100
Income from House Property		3,900

Q. No. 6

Compute the income from house property from information given below:

	Rs.
Municipal Rental value	18,000
Rent received during the year	24,000
Municipal Taxes (50% paid by tenent)	1,800 p.a.
Expenses incurred on repairs	
(*a*) by owner	3,000
(*b*) by tenent	3,000
Collection charges	1,000

Date of completion of house 1.6.91

[Hint: Net A.V. Rs. 22,500; Repairs & Collection Charges Rs. 4,500; Income Rs. 18,000]

2. Insurance Premium. The amount of any premium actually paid to insure the let-out property against the risk of damage or destruction is fully allowed as

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deduction. The mere fact that the insurance premium has become due and mere accepting the liability to pay insurance premium will not entitle the owner to claim deduction. The deduction will, therefore, be allowed in the previous year in which the premium is actually paid.

3. Annual Charge. Where the let-out house property is subject to annual charge (not being a charge created by the assessee voluntarily or a capital charge) the full amount of such charge is an admissible deduction. No deduction of annual charge shall be allowed if it is paid outside India unless tax is deducted at source.

Capital Charge means a charge to secure the discharge of a liability of a capital nature and is not allowed. [Section 27(v)]. Similarly, a self-created charge is also not allowed.

Annual Charge means a charge to secure an annual liability, but does not include any tax in respect of property or on income from property imposed by a local authority, or the Central or a State Government. [Section 27(iv)].

4. Ground Rent. Where the let-out house is subject to some sort of ground rent, the full amount of such rent is allowed as deduction. Ground rent is also payable when the land, on which the house is constructed, is taken on lease. Land revenue and any other taxes levied by the State Govt. in respect of the house property are allowed deduction on due basis, *i.e.,* whether actual payment is made or not.

5. Interest on Borrowed Capital. Where the money is borrowed for the purchase, repairs, construction, renovation etc., of the house property, the full amount of interest payable on such borrowed money is an allowable deduction. Deduction on account of interest shall not be allowed if it is paid outside India unless tax is deducted at source.

Interest on mortgage is *not allowed as deduction unless amount is borrowed for the purpose of construction, repairs, purchase or renovation* of the house. The borrowed money must be used on the house, the income of which is being calculated.

According to a board's circular, any interest paid on a loan raised to repay the loan used for construction, purchase etc., of the house is an allowable deduction. Deduction is allowed on the *accrual or due basis.*

Interest on delayed payment of interest is not allowed to be deducted. *[Shew Kisien Bhattar v.s C.I.T. (1973) 89 ITR 61 (S.C.)]*

In case interest has been paid on loan taken for construction of house or acquiring a house, prior to the previous year in which such property is acquired or constructed, it shall be allowed as deduction in five equal instalments from the previous year in which house has been constructed or acquired.

6. Land Revenue and Property Tax. The sums actually paid as land revenue or any other tax levied by the State Government in respect of the let-out property is an allowable deduction. Property tax on urban property comes under the category of tax levied by the State Government. *Proof of payment is a must and deduction is allowed on furnishing of such proof.*

7. Collection and Legal Charges. (Deleted from assessment year 1993-94).

8. Vacancy Allowance [Section 24(i)(ix)]. "Where the property is let and was vacant during a part of the year, then part of the annual value which is proportionate

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to the period during which the property is wholly unoccupied or, where the property is let out in parts, that portion of the annual value appropriate to any vacant part, which is proportionate to the period during which such part is wholly occupied is allowed as deduction."

Simply it means that the vacancy allowance shall be allowed at the rate of proportionate annual value.

In case of a house which is under self-occupation but *is deemed to be let out* no deduction of vacancy allowance is admissible as he keeps the house intentionally vacant.

The Finance Act (2) 1977 has introduced an explanation to this provision. As per this explanation the deduction under this clause shall be made irrespective of the fact whether the period during which the property or, *or as the case may be,* part of the property was vacant precedes or follows the period during which it is let.

9. Unrealised Rent. The assessee will be allowed a deduction of unrealised or unrecovered rent from the tenants provided the following conditions as laid down in Rule 5 are satisfied:

(*a*) the tenancy is *bona fide*;

(*b*) the defaulting tenant has vacated or steps have been taken to compel him to vacate the property;

(*c*) the defaulting tenant is not in occupation of any other house of assessee;

(*d*) the assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or has satisfied the Assessing Officer that legal proceedings would be useless; and

(*e*) the annual value of the house property to which the unpaid rent relates has been included in the assessed income of the previous year during which that rent was due and tax has been duly paid on such assessed income.

The deduction to be allowed on this account shall not exceed the income from the house property computed without making this deduction. In case of unrealised rent, there can be no loss. The amount of deduction of unrealised rent cannot exceed the amount of available income under the head "Income from house property". The balance of the unrealised rent, if any, is allowed to be carried forward to be set off from income of house property till it is fully exhausted. *[C.I.T. v. Madho Prashad Jetia (1976) I.T.R. 1977 (S.C.)].*

Unrealised rent allowed earlier but recovered later on [Section 25A]. With effect from assessment year 1985-86, any amount of unrealised rent which has been claimed as deduction, in any of the earlier previous years is recovered in any of the subsequent previous years, the amount so realised shall be deemed to be the income chargeable to tax in the year in which such rent is recovered. The person may or may not be the owner of the property in that year.

Loss from House Property [Section 71(1), 71(2) or 71(4)]

1. *Self occupied House whose Annual value is reduced to Nil:* Loss due to interest on loan taken to repair, renovate, construct or purchase the house can be set off from income from another house or income under any other head.

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2. *Any other house:* Loss from any other house can be set off from income of another house or income under any other head.
3. *C/F of Loss:* No loss under the head house property can be carried forward.

Illustration 7. Compute the total income of Mr. Reddy from the particulars given below for the previous years 1996-97 and 1997-98:

House Property	Previous year (1996-97)	Previous year (1997-98)
	Rs.	Rs.
(*i*) Self occupied house		
Interest on Loan	(–) 5,000	(–) 5,000
(*ii*) Let out house		
Interest on Loan	(–) 16,000	Nil
Loss due to other expenses	(–) 20,000	Nil
Income from other sources	+ 11,000	+ 11,000

Solution : *Computation of total income*

Assessment year 1997-98 (Previous year 1996-97)

	Rs.	Rs	Rs.
House Property			
Self occupied House			
Interest on Loan to be set off from other heads		(–) 5,000	
Let out house			
Loss due to interest on Loan	16,000		
Loss due to other expenses	20,000		
To be set off from any other head — Loss under the head House Property		(–) 36,000	(–) 41,000
Other sources			
Income from other Sources			(+) 11,000
Total Income			NIL

Loss of Rs. 30,000 under the head house property cannot be carried forword.

Assessment year 1998-99 (Previous year 1997-98)

House Property	Rs.
Loss from Self occupied House	(–) 5,000
Other Sources — Income	+ 11,000
Total Income	6,000

Note : Carry forward of losses has been disallowed from assessment year 1995-96 onwards.

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Q. No. 7

From the particulars given below compute total income of Mr. P. Aggarwal for the assessment years 1997-98 and 1998-99: The house was completed on 1.9.91.

	Assessment year 1997-98	Assessment year 1998-99
A. *Self occupied house*	Rs.	Rs.
Municipal Rental value	12,000 p.a.	12,000 p.a.
Fair Rental value	18,000 p.a.	18,000 p.a.
Municipal Taxes	1,200 p.a.	1,200 p.a.
Ground Rent	500 p.a.	500 p.a.
Interest on Loan	10,000 p.a.	10,000 p.a.
B. *Let out house*		
Municipal Rental value	24,000 p.a.	24,000 p.a.
Actual Rent Received	30,000 p.a.	30,000 p.a.
Municipal Taxes	2,400 p.a.	2,400 p.a.
Interest on Loan for the Previous Years		
1997-98	—	6,000
1996-97	10,000	—
1995-96	15,000	—
1994-95	15,000	—
1993-94	15,000	—
1992-93	15,000	—
1991-92	15,000	—
1990-91	15,000	—
Ground Rent	2,400	2,400
Fire Insurance Premium	2,000	2,000
C. *Income from other sources*	11,000	50,000

[**Hints:** *Assessment year 1997-98* —Loss from self occupied house Rs. 10,000; Income from letout house Rs. 6,480 Loss from HP Rs. 3,520 to be set off from other heads; Total Income Rs. 7,480.

Assessment year 1998-99—Loss from self occupied house Rs. 10,000; Income from let out house Rs. 11,680; Total Income Rs. 51,680] [P-20]

CHART SHOWING COMPUTATION OF INCOME FROM HOUSE PROPERTY

Item	*Treatment*
I—Common Steps for Gross Annual Value	
1. Adoption of Rental Value	Out of (*i*) Municipal Rental Value; (M.R.V.); (*ii*) Actual Rental Value; or (*iii*) Fair Rental Value, whichever is higher is to be adopted as Annual Rental Value (A.R.V.)
2. Local Taxes (Municipal Tax/Water Tax/Fire Tax/Educational cess etc.)	The Municipal Taxes *actually paid by owner* are allowed to be deducted in full out of A.R.V.
3. Cost of Facilities Provided by assessee to the tenants	Cost of facilities *e.g.*, (*i*) Lift Maintenance expenditure, (*ii*) Lighting of stairs, (*iii*) provision of gardener and watchman, etc. are deducted in full and balance is called actual rent.

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Balance of A.R.V. after deducting taxes is called Gross Annual Value.

II—Adjustment of Gross Annual Value

1. Let-out House

New Construction Allowance/or Statutory Allowance—[(u/s 23(1)]

(For house whose construction started after 31.3.61 and completed after 31.3.82 but before 1.4.92) Out of Gross Annual Value of the house a deduction of Rs. 3,600 p.a. per unit or Gross Annual Value whichever is less is allowed for a period of 60 months from the date of completion of house. This deduction is to be allowed only if the house is let-out for residential purposes.

2. Self-occupied Houses

One self-occupied house is exempted and A.V. is reduced to Nil. If assessee owns more than one house and claims as self-occupied then only one house of his own choice shall be exempted and other houses shall be deemed to be let-out.

3. Part of the year let out and part of the year self occupied

(*i*) Treat it as let out for full year and compute gross AV.

(*ii*) Reduce it in proportion of the period it is self occupied.

(*iii*) Out of balance allow NCA for number of months it is actual let out.

(*iv*) Total of all deductions admisible u/s 24 cannot exceed Net A.V.

4. Co-owners

If a self occupied house property is owned by co-owners, they shall be individually entitled to claim exemption u/s 23(2) for their respective portions.

5. Vacant Self-occupied House

If an assessee has reserved one house for his own occupation and that remains vacant because he is living at another place because of his employment, business, or profession, the annual value is taken to be NIL.

6. House used for assessee's own busines

Annual value of such house is taken as NIL.

7. House not in rentable condition

If the house remains vacant because of certain unavoidable reasons, *i.e.*, incompleted house or because of its situation, for whole of the year, the annual value, for such house shall be taken to be nil. In such case no loss can be returned.

8. Deemed to be Let-out

Treated as let-out, NCA is not allowed.

After adjustment whatsoever amount is left is called Net or Adjusted Annual Value.

III—Deductions from Net Annual Value [Section 24(1)]

(*a*) Self-occupied House

Only one deduction of interest on loan taken to purchase, repair, renovate or construct the house is allowed upto Rs. 15,000 or actual interest whichever is less. As a result, there shall be loss which can be set off from other houses or from any other head.

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Item	*Treatment*
(*b*) Let-out Houses	
1. Repairs & Collection Charges	1/5th of annual value.
2. Fire Insurance Premium	Full amount is allowed as deduction, if actually paid.
3. Annual Charge	Revenue or Legal charge is allowed as deduction. Capital or self-created or voluntary charge is not allowed.
4. Ground Rent	Allowed in full
5. Interest on Borrowed Capital/Interest on Mortgage	If a loan is taken to purchase, construct or renovate or repair a house and interest is paid on such loan, full amount of interest paid is allowed as deduction. Interest on Mortgage will be allowed only if purpose of loan is relating to construction, repair or renovation of house.
6. Land Revenue or any other tax levied by State Govt.	Allowed in full if actually paid.
7. Vacancy Allowance	If a let-out house remains vacant for some period during the previous year, a deduction of proportionate Annual Value (*e.g.*, if vacant for 3 months 1/4th of A.V.) is allowed.
8. Unrealised rent	The amount of unrealised rent is allowed as deduction subject to rules as given in the text. Deduction on account of unrealised rent cannot exceed income from all the house properties. Unadjusted unrealised rent can be C/F. Unrealised rent recovered later on is deemed to be the income from such house.
IV—Important Notes	
1. No deduction of interest and annual charge	If interest or annual charge is paid to a person who is not a resident and neither he himself is assessee nor there is any agent responsible to pay tax on his behalf, the deduction on account of interest or annual charge is not allowed.
2. Joint Expenses	If somewhere expenses are given jointly for two or more houses, these will be apportioned on some common basis and generally Municipal Rental Value serves as common basis.
3. Loss from House Property	(*i*) Loss from house property can be set off from income under any other head. (*ii*) Loss from self occupied house due to interest on loan can be set off from any other head.

Illustration 8. Shri Barua constructed one house in 1960. 50% of the property is let out and 50% is occupied for his residence. The letout portion was also self occupied for 2 months. The particulars are:

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	Rs.
Municipal Value	5,000 p.a.
Rent received	4,000 p.a.
Municipal Taxes	1,000
Ground rent	100
Repairs	900
Fire Insurance Premium—	200
Collection Charges	300
Interest on loan taken for construction	1,000

His income from all other sources amounts to Rs. 12,000.
Determine his income from house property.

Solution. *Computation of house property income of Mr. Barua*

	Rs.	Rs.
Municipal Rental value Rs. 5,000		
Actual Rent (4,000 × 2/1) Rs. 8,000		
Whichever is higher is ARV		8,000
Less: Municipal Taxes		1,000
Gross A.V.		7,000
Reduced to NIL for 1/2 portion being self occupied		3,500
		3,500
Further reduced for 2 months being self occupied [(3500 × 2/12)]		583
Net Annual Value		2,917
Deductions:	Rs.	
(*i*) Repairs and collection charges 1/5th of 2,917	583	
(*ii*) Ground rent	100	
(*iii*) Fire Insurance Premium	200	
(*iv*) Interest on loan	1,000	
		1,883
Income from House Property		1,034

Illustration 9. An assessee is the owner of two houses, namely:

(*i*) A kothi, the annual value of which according to the Municipal records is Rs. 12,000 but which is let out on a rent of Rs. 10,000 a year to a tenant who has undertaken to bear the cost of repairs. Municipal Taxes paid amounted to Rs. 500.

(*ii*) A shop, the annual value of which according to the Municipal records is Rs. 5,000. It is, however, let out on an annual rent of Rs. 3,500 to a tenant who has undertaken to bear the cost of repairs. Municipal taxes paid amounted to Rs. 200.

Calculate the assessee's income from house property.

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Solution

Calculation of house property income of the assessee

	Rs.	Rs.
Kothi:		
Municipal value	12,000	
Less: Municipal Taxes	500	
Annual Value	11,500	
Deductions:		
Repairs and collection charges— 1/5th of Annual Value	2,300	
Income from Kothi		9,200
Shop:		
Municipal Value	5,000	
Less: Municipal Taxes	200	
Annual Value	4,800	
Deductions:		
Repairs and collection charges— 1/5 of Annual Value	960	
Income from shop		3,840
Income from House Property		13,040

Illustration 10. Find out the taxable income from property of Sri Gyan Parkash of Amritsar from the following particulars:

He owns three houses, the municipal valuation of which is Rs. 2,000, Rs. 4,800 and Rs. 1,200 respectively. The following are further details about three houses:

(*i*) The first house built in 1955, has been let out on a monthly rent of Rs. 250. The expenses in connection with this house were: Interest on Mortgage Rs. 1,200; Land Revenue Rs. 20; Fire Insurance Premium Rs. 150; Interest on loan for the construction of the house Rs. 600; Municipal Taxes Rs. 300. The house remained vacant for two months. Unrealised rent amounts to Rs. 2,000, I.T.O. has been satisfied about this.

(*ii*) The second house was built in 1952 and is used for residential purposes. In connection with this house Rs. 300 were spent on repairs and Rs. 100 were paid as Fire Insurance Premium. The house remained vacant for three months as the owner had to stay in Bombay in a rented house in connection with his profession.

(*iii*) The construction of third house was completed on 30th June 1991 and from 1st July 1991 it was let out for residential purposes on a rent of Rs. 4,400 p.a. Municipal Tax Rs. 170 and interest on loan Rs. 2,560 were paid.

His income from there sources amounted to Rs. 12,000.

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Solution. *Computation of income from house property of Sri Gyan Prakash of Amritsar*

	Rs.	Rs.	Rs.
1st House:			
Annual rental value		3,000	
Less: Municipal Taxes		300	
Annual Value		2,700	
Deductions:			
1/5 of Annual Value as repairs	540		
Land Revenue	20		
Fire Insurance Premium	150		
Interest on loan taken for construction of the house	600		
Vacancy allowance (2 months) (2/12 × 2,700)	450		
		1,760	
Available Income		940	
Less: Unrealised rent		(–) 2,000	
Balance to be adjusted			(–) 1060
3rd House:			
Rental value		4,400	
Less: Municipal Taxes		170	
Gross Annual Value		4,230	
Less: New Construction allowance (3 months)		900	
Net Annual Value		3,330	
Deductions:			
1/5th of Annual Value as repairs	666		
Interest on loan (for construction)	2,560		
		3,226	
Income from 3rd house			104
2nd House: Self occupied			
Municipal Rental Value	4,800		
Less: M. Taxes	NIL		
Gr. A.V.	4,800		
Reduced to NIL u/s 23(2)	4,800		
	NIL		
House Property Income			NIL

Unadjusted unrealised rent of Rs. 956

Illustration 11. A is the owner of 4 houses. One house is let to a tenant for Rs. 3,000 p.a. The second house, the municipal valuation of which is Rs. 4,500 p.a. is in his own occupation. The third house remained vacant throughout the whole year as it was not in rentable condition. The fourth house, the municipal valuation of which is Rs. 6,000 is used by A for his business.

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His expenses in respect of these houses are as follows:

	Rs.
Interest on loan taken to repair the residential house	400
Fire Insurance premium for 1st, 2nd and 4th house	1,410
Collection charges	350
Ground rent in respect of 2nd house	200

The first house, which is let, remained vacant for two months. Calculate A's income from house property.

Solution

Computation of House Property income of Mr. A

1st House: Let out

	Rs.	Rs.
Annual Rental Value	3,000	
Less: Municipal Taxes	—	
Annual Value		3,000
Deductions:		
1/5th of annual value as repairs and collection charges	600	
Fire Insurance Premium [2 : 3 : 4]	313	
Vacancy allowance (2 months) (2/12 × 3,000) (Calculated as per provisions of law)	500	
		1,413
Income from 1st House		1,587

3rd House:

This house was not in rentable condition throughout the year as given in the question, so the annual value of this house is taken as nil. There can be no loss in this case.

4th House:

This house is being used for assessee's business. So no income will be taken under this head of 'Income from House Property'. Its income and expenses are treated under the business head of income. This house is outside the purview of this head of income.

2nd House: Self-occupied

	Rs.
Municipal Rental Value	4,500
Less: Municipal Taxes	NIL
Gross Annual Value	4,500
Reduced to NIL u/s 23(2)	4,500
Net A.V.	NIL
Less: Interest as Loan	(–) 400
Loss from self-occupied House	400

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House Property Income	Rs.
1st House	1,587
2nd House (Loss)	– 400
3rd House	—
4th House	—
Total	1,187

Illustration 12. An assessee owns four house properties of which he uses one (No. IV) for his residence. The following are the particulars in respect of the properties. Compute the assessee's income from house property.

	I	II	III	IV
When constructed	1948	1963	31st May 1991	1973
Municipal Value	10,000	12,000	2,700	8,000
Rent received	12,000	10,000	3,600	—
Local Taxes	500	600	45	200
How used	Let-out for business	1/2 usedfor own business, 1/2 given to the manager of the concern	Let-out for residential purpose	Self-occupied
Actual repairs	500	500	200	100
Interest on mortgage	—	—	500	—
Ground rent	50	—	30	—
Fire insurance premium	—	100	—	120
Vacancy	2 months	—	one month	—
Collection charges	500	20	30	—
Annual charges	—	180	—	—

Notes. 1. Property No. III consists of 2 residential units of equal municipal value and given rental values are for both the units.

2. Assessee's total income from other sources is Rs. 15,000.

Solution

Computation of assessee's income from house property

1st House	Rs.	Rs.
Annual Rental Value		12,000
Less: Municipal Taxes		500
Net Annual Value		11,500
Deductions:		
Repairs and Collection Charges—		
1/5th of Annual value	2,300	
Ground rent	50	
Vacancy allowance (2 months) ($^2/_{12} \times 11{,}500$)	1,917	
		4,267
Income from 1st house		7,233

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2nd House

Used for own business. Hence, Annual Value is Nil. House given to manager is also considered to be used for business.

3rd House (Date of completion 31.5.1991)

Rental value of 2 residential let-out units		3,600
Less: Local taxes		45
Gross Annual Value		3,555
Less: New construction allowance @ Rs. 3,600 for each unit for 2 months Rs. 1,200 but restricted to $^{2}/_{12}$ of Gross Annual Value *i.e.* Rs. 593		593
Net Annual Value		2,962
Deductions:		
Repairs and Collection charges		
1/5th of N.A.V.	592	
Vacancy 1/12 of N.A.V.	247	
Ground rent	30	
		869
Loss from House		2,093

4th House (Self-occupied):

Municipal Rental Value	8,000
Less: Municipal Taxes	200
Gross A.V.	7,800
Reduced to NIL u/s 23(2)	7,800
Net A.V.	NIL

Income from House Properties:

	Rs.
1st House	7,233
2nd House	Nil
3rd House	2,093
4th House	Nil
Total	9,326

Illustration 13. Mr. P is the owner of a house property in Kanpur. It has been let out for Rs. 90,000. The tax payable by the owner comes to Rs. 8,400 on municipal valuation of Rs. 84,000 but the landlord has taken an agreement from the tenant stating that the tenant would pay tax direct to the municipality. The landlord, however, bears the following expenses on tenant's amenities:

	Rs.
Water charges (as per agreement)	1,000
Lift Maintenance	1,000
Salary of Gardener	1,200
Lighting of Stairs	800

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The landlord claims the following deductions:

Repairs	30,000
Land Revenue	1,000
Collection Charges	2,000

Legal charges incurred on purchase of land on which house property is situated Rs. 24,000.

Compute the taxable income from house property. *(P.U. B.Com.)*

Solution

Computation of Income from House Property of Mr. P.

	Rs.	Rs.
Actual rental value		90,000
Deduct: Expenses met by landlord on amenities provided to the tenants:		
1. Water Charges	1,000	
2. Lift Maintenance	1,000	
3. Salary of Gardener	1,200	
4. Lighting of Stairs	800	
		4,000
		86,000
Net Annual Value (M.R.V. Rs. 84,000 or Rs. 86,000, *w.e.* is higher)		86,000
Deductions:		
(*i*) 1/5th for Repairs and collection charges	17,200	
(*ii*) Land Revenue	1,000	
		18,200
Taxable Income from Property		67,800

Note: Legal charges incurred on purchase of land are capital expenses, hence disallowed.

Illustration 14. A house was completed on April 1, 1996 and following information is available about this house:

	Rs.
Municipal Value of the House	36,000 p.a.
Fair Rental Value of the House	35,000 p.a.
Actual Rent	3,000 p.m.
Municipal Taxes	6,000 p.a.

Let out for the period 1.4.96 to 30.6.96 and self occupied from 1.7.96 onwards.

	Rs.
Fire Insurance Premium	3,600
Land Revenue	6,000
Interest on Loan for the period	

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(*a*) 1.4.93 to 31.3.96 45,000
(*b*) 1.4.96 to 31.3.97 15,000

Calculate income from the house property for the previous year ending on 31.3.1997.

Solution

Computation of Income from House Property

	Rs.	Rs.
Municipal Rental Value	36,000	
Fair Rental Value	35,000	
Actual Rental Value	36,000	
Whichever is higher is A.R.V.		36,000
Less: Municipal Taxes		6,000
Balance		30,000
Less: Proportionate Annual value for the period house was self-occupied (9/12 of 30,000)		22,500
Net Annual Value		7,500
Deductions u/s 24		
Repairs 1/5th	1,500	
Fire Insurance Premium	3,600	
Land Revenue	6,000	
Interest on Loan for the year	15,000	
Interest on Loan for the period 1.4.93 to 31.3.96 (45,000 × 1/5)	9,000	
Total deductions	35,100	
Restricted to Net Annual Value		7,500
Income from H.P.		NIL

Note: The house property is covered u/s 23(2)(a)(ii), *i.e.*, part of the year let-out and part of the year self-occupied is not subject to restriction on deduction regarding interest on Loan—upto Rs. 10,000 only. It is to be treated as Let-out for all purposes except reduction in annual value and restriction on total amount of deductions.

Illustration 15. From the particulars given below compute income from house property:

Date of Completion	1.11.91
Municipal Rental Value	Rs. 30,000
Fair Rental Value	Rs. 24,000
Self-occupied	2/3 portion

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Let-out	1/3 portion from 1.4.96 to 31.8.96 @ Rs. 1,000 p.m. and self-occupied from 1.9.96 onwards.
Municipal Taxes	Rs. 3,000 p.a.
Fire Insurance Premium	Rs. 2,000 p.a.
Ground Rent	Rs. 4,000 p.a.
Interest on Loan	Rs. 7,500.

Solution. *Computation of House Property Income*

	Rs.	Rs.
Municipal Rental Value	30,000	
Fair Rental Value	24,000	
Actual rent it can fetch (1,000 × 12 × 3/1)	36,000	
Annual Rental Value (Treating as fully let-out during the year)		36,000
Less: Municipal Taxes		3,000
Gross Annual Value		33,000
Reduce 2/3 being self-occupied		22,000
		11,000
Reduce further for 7 months for which 1/3 is self-occupied (7/12 × 11,000)		6,417
Adjusted Annual Value		4,583
Less: New Construction Allowance (5 months)		1,500
Net Annual Value		3,083
Deductions:		
Repairs 1/5th	617	
Fire Insurance Premium	2,000	
Ground Rent	4,000	
Interest on Loan	7,500	
Total	14,117	
But restricted to Net Annual Value		3,083
Income		NIL

Q. No. 8

A building was constructed in 31st July 1991. During the previous year 1995-96 it was let out at an annual rent of Rs. 15,000. The fair rent at which it could be let out was Rs. 20,000. The municipal tax for the property amounted to Rs. 2,000 and it was paid as under:

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Case I : Owner paid Rs. 1,000 and the Occupier Rs. 1,000.

Case II : Owner paid Rs. 2,000.

Case III : Owner paid Rs. 1,200 and the Occupier paid Rs. 800.

Case IV : Occupier paid Rs. 2,000. (Let out for business of occupier).

What is the adjusted annual value in each of these cases?

[**Hints:** Case I: Rs. 17,800, Case II: Rs. 16,800, Case III: Rs. 17,600, Case IV: Rs. 20,000 (No deduction of taxes]

Q. No. 9

Mr. X, the owner of two houses, occupies one for his own residence and the other he lets to a tenant at a monthly rent of Rs. 500. The municipal valuation of the house occupied is Rs. 2,600 and of the other is Rs. 5,200. The municipal taxes of the two amounted to Rs. 600. The other expenses in respect of the two houses are as follows:

	Rs.
Insurance premium (for both houses)	1,200
Annual charge in respect of the house occupied	300
Ground rent for the house let	100
Repairs of the house occupied	700
Interest on loan taken to repair the two houses	400

Mr. X also had income from other sources amounting to Rs. 20,000 during the year. Calculate Mr. X's income from house property and total income.

[P.U. B.Com. (Supp.) 1975]

[**Hints:** Let-out Rs. 3,313, Self-occupied Loss Rs. 133. Total Income Rs. 23,180]

Q. No. 10

Shri M.D. Arora is owner of two houses. In respect of these he has furnished following particulars:

	House A	*House B*
Date of completion of construction	*31.12.91*	*1st July 1996*
Municipal Rental Value	3,600 p.a.	
Actual Rent Received	3,000 p.a.	600 p.m.
Municipal Taxes	360	
Ground Rent	—	600
Collection Charges	100	180
Interest on loan taken	—	220

Compute his income from house property.

[**Hints:** House A: N.C.A. Rs. 2,430: Income Rs. 648 House B: Income Rs. 3,500, Income from House Property Rs. 4,148]

Q. No. 11

Mr. Chopra draws a salary of Rs. 1,000 p.m. He owns two houses: one whose municipal valuation is Rs. 3,000, is occupied by him for his own residence and the other, whose municipal valuation is Rs. 2,500, is let out at Rs. 250 p.m. The expenses in respect of both the houses are:

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	1st House (occupied for *own residence)*	*2nd House* (let-out)
	Rs.	Rs.
Municipal taxes	300	300
Land revenue	150	200
Interest on loan for reconstruction of the houses	300	400
Fire Insurance premium	200	200
Interest on mortgage	—	500
Rent collection charges	—	200

The 2nd house remained vacant for two months. His income from other sources is Rs. 5,000.

Compute his total income. *[B.Com. (Hons.) Delhi].*

[**Hints:** Let-out house Rs. 910; Self-occupied loss Rs. 300; Salary income Rs. 8,000: Total Income Rs. 13,610] [P-2].

Q. No. 12

Mr. Raja Ram owned four houses. Their municipal valuations are Rs. 6,000 Rs. 6,000 Rs. 5,500 and Rs. 10,000 respectively. The municipality levies 10% tax. The first house is occupied for his residence. Hari Ram is residing in the second house at a monthly rent of Rs. 800. The third house is occupied by a business-house at an annual rent of Rs. 6,600. In the fourth house Raja Ram is carrying on his own business which has yielded a net taxable income of Rs. 15,145. The second and third houses were constructed on 30.6.1991.

He claims the following deductions:

Interest on mortgage of the first house Rs. 200.

Rs. 600 paid as salary to a gardener in respect of the third house.

Compute the taxable income from house property.

[**Hints:** Let-out (2nd house) Rs. 6,480; 3rd house Rs. 4,360; 4th house Nil as house used for assessee's own business. Self-occupied (1st house) Nil u/s 23(2); Income from House Property: Rs. 10,840, No. N.C.A. in 3rd house as it is let out for non-residential purposes].

Q. No. 13

Mr. Parampal Singh owns a house property at Chandigarh. It was completed on 1.11.95 and is used as follows :

(*a*) 25% of floor area is used for his own business.

(*b*) 25% of floor area is self occupied for his own residence.

(*c*) 25% of floor area is let out for residential purpose @ Rs. 1,000 p.m.

(*d*) 25% of floor area was let out for non residential purposes @ Rs. 1,000 p.m. with effect from 1.4.96 to 29.2.97 and self occupied from 1.3.97 onwards.

The other expenses incurred by Mr. Singh is respect of house property are :—

Municipal Taxes Rs. 4,000 p.a.

Fire Insurance Premium Rs. 1,200 p.a.

Repairs of House Property Rs. 3,200 p.a.

Compute income under the head house property for the assessment year 1997-98.

[**Hints :** To be treated as one house : 1/4th used for business NIL : 3/4th for residential—Net A.V. 21,083, Income from House Property Rs. 15,966] [P-19].

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Q. No. 14

Mr. Srikant owns two houses, one house of the municipal valuation of Rs. 10,000 p.a. is occupied by him for his own residence and the other whose municipal valuation is Rs. 8,000 p.a. is let out for Rs. 500 p.m. The yearly expenses in respect of both the houses are as under:

	Self-occupied Rs.	*Let-out* Rs.
1. Municipal taxes	1,000	800
2. Interest on loan:		
(*a*) taken for purchase of the house	—	1,000
(*b*) taken for the marriage of his daughter	800	
3. Collection charge		500
4. Annual charge		500

The let-out house remained vacant for one month during the previous year. Srikant was having income from other sources Rs. 10,000.

Compute his taxable income from House property for the assessment year 1997-98. *[Calcutta University B.Com. Pass]*

[**Hints:** Income from let-out house Rs. 3,660, Self-occupied NIL u/s 23(2)],

Q. No. 15

The particulars of a residential house completed on 31st May 1991 are given below:

	Rs.
Annual rent	9,600
Municipal taxes paid	1,800
Ground rent	50
Insurance	80
Interest on amount borrowed for construction of this house	1,000
Collection charges actually paid	300

The assessee mortgaged the house for Rs. 36,000 to meet the expenses of his daughter's marriage and paid an interest of Rs. 3,000 on the mortgage loan during the year. The assessee also claimed that he had not realised rents from his tenants for earlier years to the extent of Rs. 8,000 and he proved his claim to the entire satisfaction of the assessing officer that the conditions for its admissibility were satisfied.

Compute the total income of the assessee for the year.

[B.Com. Punjab]

[**Hints:** Income—Nil. Unadjusted rent (Rs. 3,370) will be c/f to be set off against House property income of assessee in succeeding previous years till it is fully exhausted] [P-5].

Q. No. 16

Shri Ashish owns a house property. Its annual letting value is Rs. 8,100. During the previous year, it was let out to a tenant on a monthly rent of Rs. 450. The tenant defaulted in the payment of rent for three months. The legal proceedings instituted in a court of law for the recovery of rent have not been disposed of. Shri Ashish has claimed the following expenses:

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	Rs.
(*a*) Municipal taxes	2,400
(*b*) Legal expenses for recovery of rent	600
(*c*) Maintenance allowance paid to step-mother which was annual charge on the property according to his father's will	900

Compute the income from house property of Shri Ashish for the current assessment year.

[**Hints:** Net A.V. Rs. 5,700; Income Rs. 3,660; No deduction of unrealised rent as it relates to current previous year and the legal proceedings have not yet been disposed of]

Q. No. 17

Mr. Z is the owner of the three buildings. First building is let out at Rs. 500 p. m., Municipal Valuation—Rs. 5,600. The second building, is occupied by Mr. Z for his residential purpose. Municipal value is Rs. 5,400 p.a. Municipal taxes paid are equal to 10%, 15% and 10% of the Municipal valuation respectively. All the houses were constructed in 1956. His third house property (Municipal value Rs. 600) is situated in Kanpur and which could not be occupied during the whole year by Mr. Z because of his business in Calcutta.

The following are details of expenses, incurred for the three buildings:

	Property		
	I	*II*	*II*
	Rs.	Rs.	Rs.
Repairs	1,200	600	100
Interest on mortgage of loan taken for the marriage of his daughter	1,000	—	—
Vacancy Allowance	2 months	—	—
Land Revenue	50	20	—
Fire Insurance Premium	200	150	—
Collection charges	800	250	—

The only other income of Mr. Z for the year ended 31st March 1997 was Rs. 3,200 from his own business of cotton textiles at Calcutta. He has paid Life Insurance Premium of Rs. 1,000 on his own life.

You are required to compute the total income of Mr. Z for the current assessment year.

[**Hints:** Property I: Rs. 3,195, Property II: Rs. NIL ; Property III: Rs. 432. Income of Property III to be computed as let-out house as he has more than one house as self-occupied and cannot get the benefit of vacancy of self-occupied house; Total Income Rs. 6,827 Q.A. for rebate u/s 88 Rs. 1,000 [P-7].

Q. No. 18

Compute income from house property from the particulars given below for the assessment year 1997-98 :—

	Rs.
Municipal rental value	24,000 p.a.
Actual rent received	30,000 p.a.
Municipal taxes	2,400 p.a.

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Date of completion	31.3.1996
Date of letting	1.4.1996
Fire insurance premium (due)	400 p.a.
Ground rent (due)	600 p.a.
Interest on loan taken to construct the house	
1994-95	15,000
1995-96	15,000
1996-97	10,000
Interest on delayed payment of interest	1,000
Unrealised rent recovered	6,000

(Out of this only Rs. 3,000 were allowed during assessment year 1995-96)

[**Hints :** Income from house 5,480 previous year 1995-96 is included in pre-construction period. unrealised rent recovered Rs. 3,000 Interest on delayed payment not allowed] [P-22]

Q. No. 19

Mr. Ram Niwas constructed a house which was completed on 1.3.1992 and let out from 1.4.92 @ Rs. 450 p.m. Its municipal value was assessed to Rs. 2,400 p.a. on which local taxes were charged @ 10%. He paid Rs. 100 as ground rent, Rs. 100 as Fire Insurance premium and Rs. 200 as collection charges. He had taken a loan of Rs. 40,000 @ 9% to construct this house. His income from all other sources is Rs. 69,500. Compute his total income for the previous year ending on 31.3.97.

[**Hints:** Loss of Rs. 2,312 to be set off. Total Income Rs. 69,500 – 2,312 = 67,188]

Q. No. 20

Mr. Ray, who has income only from house property, submits the following information about his house property income:

	Rs.
Gross Rental income of the year (after deducting following items)	1,00,000
(*i*) Depreciation	24,500
(*ii*) Lift maintenance charges	7,500
(*iii*) Municipal Taxes (10% of MRV of Rs. 1,50,000)	15,000
(*iv*) Vacancy	10,000
(*v*) Repairs	18,000
(*vi*) Pay of chowkidar	1,000
(*vii*) Bank commission	500
(*viii*) Legal expenses on recovery of rent	8,000
(*ix*) Salary of gardener	1,200

Compute Mr. Ray's income from house property for the previous year ending on 31.3.97.

[**Hints:** Annual Rent Rs. 1,85,700; Annual Value Rs. 1,61,000 Income Rs. 1,18,800]

Q. No. 21

Following are the particulars of house properties of Mr. Vishal. Compute his income from house property:

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	I	II
Construction started on	31.3.1991	10.2.1989
Construction completed on	31.3.1992	1.6.91
	Rs.	Rs.
Actual Rent	20,000	15,000
Municipal valuation	23,200	12,000
Municipal tax	2,200	1,200
Actual repair expenses	1,700	800
Interest on moneys borrowed to renovate the building	1,200	—
Insurance premium	200	175
Ground rent	150	75
Vacancy period	3 months	Nil
Unrealised rent	2,000	Nil

Both the above houses were let out for residential purposes. *Insurance premium of the first house* and ground rent of the second house are **still outstanding.** The assessee has satisfied all the conditions regarding the unrealised rent allowance. **Repair expenses of the first house and the municipal tax of the second house were paid by the tenants.**

[**Hints:** House I: Rs. 6,220, No deduction of Insurance Premium which is still unpaid. House II: Rs. 11,270, No deduction of Municipal Taxes: Full deduction of ground rent due but not paid] [P-9].

Q. No. 22

Mr. A has the following properties:

(*i*) Flat in Bombay purchased on 1st June 1996 which is let out on a monthly rent of Rs. 2,100. The building in which the flat is located was completed *on 31st May, 1996.* The flat was let out from 1st August 1996.

(*ii*) Flat in Delhi constructed in 1992 which is self-occupied.

(*iii*) Godown in Calcutta constructed in 1992 is let out on a monthly rent of Rs. 6,000.

The expenses actually incurred during the year against rental income are:

	At Bombay	*At Delhi*	*At Calcutta*
	Rs.	Rs.	Rs.
Municipal Taxes	5,000	2,400	18,000
Building Co-operative Maintenance Charges	1,000	900	—
Electricity Charges	—	1,200	4,800
Fire Insurance Premium	—	—	600
Collection Charges	750	—	5,400
Repairs	20	1,900	11,000

The following further information is given:

(*i*) The flat in Delhi if let out would fetch a monthly rent of Rs. 4,000.

(*ii*) Mr. A carried on a business in which he suffered a loss of Rs. 10,000 during the year ended on March 31, 1997.

(*iii*) Mr. A received a consolidated salary of Rs. 6,400 p.a. during the year from a part-time employment which he holds.

Compute Mr. A's total income for the year ended on 31.3.97.

[C.A. Inter. (Adopted)]

[**Hints:** *Bombay Flat*—

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Rent for 10 months	21,000
Less: Municipal tax	5,000
Net Annual Value	16,000

Deduction of vacancy 2/10 of Net A.V. Income Rs. 9,600; Calcutta godown Rs. 42,600: Delhi self-occupied Nil: Business Loss Rs. 10,000: G.T.I. Rs. 46,467. Vacancy of let-out house may precede a tenancy or may be followed by a tenancy; deduction is allowed as per explanation attached by Finance Act (2) 1977] [P-10].

Q. No. 23

Shri Sita Ram has five houses, the municipal valuations of which are Rs. 16,000, Rs. 20,000, Rs. 12,000, Rs. 8,000, and Rs. 10,000 respectively. In the first house he runs his own business. He lives in the second house. The other three houses are let out for Rs. 800, Rs. 700 and Rs. 1,200 p.m. respectively.

One-third portion of the third house is also used for his residential purposes and rent of Rs. 800 p.m. is received for remaining two-third portion. A loan was taken for the construction of the fifth house, the construction of which began on 1st September 1991 and ended on 31st January 1992. This house was let out from 1st February 1992. For the previous year 1996-97 the interest paid by him on this loan amounted to Rs. 1,000. Municipal taxes on these houses were assessed @10% of Municipal valuation. His taxable income from business was Rs. 67,166. Compute the taxable income from house property.

[**Hints:** House I: NIL, House II: NIL, House III: Rs. 10,560; House IV: Rs. 6,080; House V: Rs. 7,320; Total Rs. 23,960]

Q. No. 24

Shri K. Chaudhary, a resident individual, owns a house in Calcutta, the municipal valuation of which is fixed at Rs. 18,000 by Calcutta Corporation after deducting 10% as an allowance for repairs from gross rental value. He has let out one-half portion of the building for Rs. 1,100 per month after the construction was completed on 31.1.1992. Compute the taxable income of Shri Chaudhary under the head 'Income from House property' from the following particulars:

	Rs.
He paid Municipal Taxes	1,200
Tenant paid Municipal Taxes	600
He spent for repairs	750
for ground rent	300
for Insurance premium (for the House)	400
for interest on loan for house construction	500
for collection charges	350
for annual charge	600

Let-out portion remained self occupied for two months (1.2.97 to 31.3.97) in the year. His total income other than from house property was Rs. 30,000 for the year.

[Adapted Calcutta University B.Com. (Hons.) 1980]

[**Hints:** H.P. Income Rs. 4,200] [P-12]

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Q. No. 25

Mr. D. Thomas has three houses in Calcutta, details of which are given below:

(*a*) House No. I constructed on leasehold land on 31.3.1992 and let out to tenant at a rent of Rs. 800 p.m. Municipal Taxes are Rs. 1,200 per year, 50% of which are paid by tenant. Repair expenses of Rs. 500 and ground rent of Rs. 900 for the year paid by Mr. Thomas.

(*b*) House No. II was taken on lease from Mr. K. David at a rent of Rs. 400 per month. *It was sub-let at a rent of* Rs. 750 p.m. *Municipal Taxes of Rs. 1,000 and* Repairs expenses of Rs. 800 for the year are paid by Mr. Thomas.

(*c*) House No. III constructed on his own land on 30th June 1991. Half of the building is occupied for his residential purpose and the other half is let out to a tenant at a rent of Rs. 350 p.m. for residential purposes. This portion was self occupied during March 97. The Municipal Value of the building is fixed at Rs. 12,900 p.a. The Municipal taxes of Rs. 1,600 were paid by Mr. Thomas. Repairing charges of Rs. 1,000 are equally met by Mr. Thomas and the tenant. Interest paid on loan taken for construction of building by Mr. Thomas is Rs. 400 for the year. Compute the gross total income of Shri Thomas for the assessment year 1997-98 assuming that his business income is Rs. 30,000. *[Calcutta University B.Com. (Hons.)]*

[**Hints:** House No. I: Rs. 3,420; House No. III: Rs. 3,023, House No. II: sub-let under the head 'Income from other sources'. Only actual expenses are allowed. Income Rs. 2,400, G.T.I. Rs. 38,843] [P-13].

Q. No. 26

Mr. X of Daryaganj, New Delhi, owns several properties which are let out to tenants. He is owner of the house in which he is living at Daryaganj and *its Municipal valuation is Rs. 9,000 p.a. From the following statement of accounts* for the year ended on March 31, 1997; compute his total income:

	Rs.		Rs.
To Municipal Taxes (60% being tenant's share)		By rent Green Park House	12,000
Green Park House	400	By rent Vasant Vihar House	24,000
Vasant Vihar House	800	By rent South Extension house (occupied for 10 months)	15,000
South Extension House	320	By rent Gupta Colony Flat (Completed on 1.10.96 Let out for residential purposes)	6,000
Gupta Colony Flat	240		
Daryaganj Bungalow	600		
To Ground rent of Gupta Colony Flat	250		
To Repairs	6,000		
To Collection Charges			
(*i*) Green Park 480			
(*ii*) Vasant Vihar 800			
(*iii*) South Extension 640			
(*iv*) Gupta Colony 480			
	2,400		

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To Interest paid to Bank (Loan taken for construction of South Extension house)	3,000	
To Life Insurance Premium	6,500	
To excess of receipts over expenses	36,490	
	57,000	57,000

Municipal valuation of the houses is: (annual) Green Park House Rs. 12,000; Vasant Vihar House Rs. 20,000. South Extension House Rs. 16,000, Gupta Colony Flat Rs. 12,000.

[**Hints:** Income from Green Park House Rs. 9,280; from Vasant Vihar House Rs. 18,560; from South Extension House Rs. 8,197 (Vacancy allowance for two months); from Gupta Colony House Rs. 4,358 and Daryaganj self-occupied NIL. T.I. 40,395] [P-15].

Q. No. 27

Mr. Mahajan Prasad owns a house in Calcutta constructed in 1991-92. The construction was completed on 31.1.92. The house consists of 4 flats of equal dimension, two of which are let out for residential purposes and the remaining two flats are occupied by the owner for own residence. The following particulars are available in respect of the house for the year 1996-97 :—

	Rs.
(*i*) Municipal value	18,000
(*ii*) Ground rent	150
(*iii*) Interest paid on capital borrowed on mortgage of the house	1,500
(*iv*) Rent per flat	3,000 p.a.
(*v*) Municipal Taxes borne by tenant for each flat for the year	240

Mr. Prasad's income from other sources for the year 1996-97 was Rs. 50,000. Compute his income from house property on the basis of above information.

[C.U.B.Com. (Hons.)]

[**Hints :** Income from letout units (2 actual + one deemed to be let Rs. 5,695; one unit self occupied NIL. Municipal taxes to be allowed out of self occupied and deemed to be let units] [P-11]

Q. No. 28

Mr. Ansari is owner of two houses and provides following informations about these houses:

	A	*B*
Date of Completion	*1.6.96*	*1.8.95*
Standard Rent	Rs. 15,000 p.a.	—
Fair Rental Value	Rs. 18,000 p.a.	Rs. 24,000 p.a.
Municipal Rental Value	Rs. 12,000 p.a.	Rs. 20,000 p.a.
Actual Rent	Rs. 12,000 p.a.	Self-occupied
Municipal Taxes	Rs. 1,200	10% of M.R.V.

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Ground rent (due)		Rs. 400	—
Fire Insurance Premium		Rs. 500	Rs. 400 p.a.
Interest on Loan for the construction of House for the year	1993-94	Rs. 4,000	Rs. 11,000
	1994-95	Rs, 4,000	Rs. 11,000
	1995-96	Rs. 3,000	Rs. 11,000
	1996-97	Rs. 3,000	Rs. 7,000

Calculate his income from the house property for the year ended 31.3.1997.

[**Hints:** Let out House A.R.V. Rs. 12,500, Deduction of Interest (3,000 + 1/5th of 11,000) Rs. 5,200 Income 2,940.]

Self-occupied A.V. is NIL; Deduction of Interest (7,000 + 1/5th of 22,000) Rs. 11,400 but restricted to Rs. 10,000. Hence loss Rs. 10,000. Loss from HP Rs. 7,060 to be adjusted from any other income.] [P-18].

Q. No. 29

The following information is given to you by Y, an individual, to enable you to prepare his statement of total income for the assessment year 1997-98. All working notes are to form part of your answers.

(*a*) (*i*) He was employed as a senior Manager of company and paid the following :

Basic Salary	Rs. 4,000 p.m.
special allowance	at 25% of the basic salary
Peon allowance	at Rs. 200 p.m.
Bonus	Rs. 20,000.

During the year, he was asked to proceed to Amritsar to manage temporarily the Branch there and was paid a special pay (not included above) of Rs. 5,000 for this assignment.

(*ii*) Three of his children were educated in Convents outside the place of his service and the employer paid an allowance of Rs. 500 per child per month to meet the costs of education and boarding expenses.

(*iii*) The employer reimbursed Y with Rs. 300 p.m. being the tution fees paid to the Institute of Higher Learning and Management where Y had enrolled himself to the M.B.A.

(*iv*) During the year, he availed himself of leavel travel concession facility for his family and himself. The travel was within the prescribed block of year. He did not travel but his wife and two major children did and performed the journey by air. The company paid Y Rs. 10,800 as leave travel concession claim. Travel by air-conditioned secod class would have cost each of the persons for the places visited Rs. 1,800 (both ways).

(*b*) Y owns two residential properties—one at his home-town which he has not been using because of his employment elsewhere and in which his parents reside—and the other at Baroda. The home-town property's annual value, as assessed by the municipality, is Rs. 3,600 and the annual municipal tax paid was Rs. 300.

The Baroda property has been let to a company for a guest house. The company pays Y an annual rent of Rs. 50,000 and also meets the municipal taxes of Rs. 18,000 per annum. The company, in addition, has undertaken to keep the premises in a fully repaired condition. The annual value assessed by the Baroda municipality for the property is Rs. 42,000.

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Y's employer deducted from his salary 10% of the basic pay towards employee's contribution to a recognised provident fund ; the employer made an equal contribution. Interest on provident fund account credited to Y's account in the year was Rs. 10,000. He deposited Rs. 5,000 in National Saving Scheme (1992) during the previous year. *[C.A. Inter Nov. 1990 (Adapted)]*

[**Hints :** Education and Boarding allowance taxable Rs. 13,200, Personal Tution fee exempted LTC exempted upto Rs, 5,400, Salary Income 91,000, Home town house (deemed to let) Rs. 2,640, Baroda House Rs. 40,000 Q. A. for rebate u/s 88 Rs. 9,800] [P-21].

QUESTIONS

1. Define 'Annual Value'. How is it determined?
2. What deductions are allowed from the annual value in computing taxable income from house property.
3. Distinguish:
   (*a*) Annual Value and Annual Rental Value.
   (*b*) Let-out and self-occupied residential properties. How would you determine the annual value of the house used by assessee for his own residence?
4. Write short notes on:
   (*i*) New construction allowance, (*ii*) Unrealised rent, (*iii*) Vacancy allowance, (*iv*) Rental value, (*v*) Repairs allowance, (*vi*) Annual Rent, (*vii*) Exempted Income from House Property, (*viii*) Deemed owner (*ix*) Annual charge and (*x*) Recovery of Unrealised Rent.

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3 PROFITS AND GAINS OF BUSINESS OR PROFESSION-I

Definition of head—Business—adventure in the nature of trade—profession—charging provisions—computation of income under this head—rules thereof—allowable expenses (Sections 30 to 37)—Expenses expressly disallowed—Expenses disallowed in certain cases—Deemed profits—Valuation of stock—Misc. provisions u/s 44—Chart—Illustrations—Questions.

DEFINITION OF HEAD (Section 28)

Under sections 28 to 44 of the Income-tax Act 1961, Profits & Gains of business or profession form part of total income of an assessee. This head is the most important source of tax collection for the Government. The computation of income under this head is a very complex and difficult method but before going into calculation of income under this head, it is necessary to understand the meaning of terms used in this head.

Business

Business simply means any economic activity carried on for earning profits. Section 2(3) has defined the term as "any trade, commerce, manufacture or any adventure or concern in the nature of trade, commerce and manufacture". In the words of Justice S.R. Dass, "The word 'business' connotes some real, substantive and systematic or organised course, activity or conduct with a set purpose".

In this connection it is not necessary that there should be a series of transactions in a business and also it should be carried on permanently. Neither repetition nor continuity of similar transactions is necessary. As already defined under section 2(3), the income derived from any adventure in the nature of trade is also treated as business income. So a brief explanation of this term is necessary.

Adventure in the Nature of Trade

Profits arising from an isolated transaction are taxable as business profits, if it is treated as an adventure in the nature of trade, commerce or manufacture. To decide whether a particular case is an adventure in the nature of trade or not depends upon the fact and circumstances of each case. The Supreme Court has summed us following *principles* to decide such case (35 I.T.R. 609).

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(*i*) Was the purchaser a trader and was the purchase of the commodity and its resale allied to his usual trade or business or incidental to it?

(*ii*) What is the nature of the commodity purchased and resold and in what quantity was it purchased and resold? If the commodity purchased is generally the subject-matter of trade and it is purchased in very large quantity, it would tend to eliminate the possibility of investment for personal use, possession or enjoyment?

(*iii*) Did the purchaser by any act subsequent to the purchase improve the quality of the commodity purchased and thereby made it more readily saleable?

(*iv*) What were the incidents associated with the purchase and resale? Were these similar to the operations usually associated with trade or business?

(*v*) Are the transactions of purchase and sale repeated?

(*vi*) In regard to the purchaser of the commodity and its subsequent possession by the purchaser, does the element of pride of possession come into the picture? If the answer to this question is 'yes' then it will not be a transaction which will make it an adventure in the nature of trade.

(*vii*) Was the purchase made with the intention to resale it at a profit? The intention of the purchase is very important at the time of purchase. If there is change of intention after some time, that will not make transaction as an adventure in nature of trade.

So, these are the important factors which are borne in mind to decide whether a particular transaction is an adventure in the nature of trade or not.

Onus to Prove. The Supreme Court (38 I.T.R. 242) held that where a transaction is not in the line of the business of the assessee but is an isolated or single instance of a transaction the onus is on the Income-tax Department to prove that the transaction was an adventure in the nature of trade.

Profession

A profession is an occupation requiring purely intellectual skill or manual skill controlled by the intellectual skill of the operator, *e.g.*, lawyer, accountant, engineer, surgeon, author etc. So profession refers to those activities where the livelihood is earned by the persons through their intellectual or manual skill. Under section 2(36) profession includes vocation.

Vocation simply means a way of living for which one has special fitness. A vocation does not involve any organized or systematic activity like business. So vocation simply means any type of activity in which a person is engaged and he earns his livelihood from such activity. The practice of a religion may also amount to vocation.[1] Any gain or receipt arising out of vocation is certainly taxable under this head of income. Writing of articles in the magazines is also a vocation.[2]

1. Govindalji Ramachandji *v.* C.I.T. (1957) 34 I.T.R. 92.
2. C. Rajagopalachariar *v.* C.I.T. (1963) 50 S.T.R. 196, 199 Madras.

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CHARGING PROVISION (Section 28)

The following are the incomes which are chargeable to income-tax under the head 'Profits and Gains of Business or Profession'.

(*i*) Business or Professional Income [Section 28(*i*)]

The profits and gains of any business or profession which was carried on by the assessee at any time during the previous year are assessed under this head. The business or profession should be carried on in the previous year and it is not necessary that it should continue throughout the year. The owner of the business is to be charged under this section, whether he may carry business personally or through a manager, agent or servant.

Business outside India and Business in India stand on the same footing for the purposes of this section.

All revenue profits arising from business or profession are chargeable even if they are of a casual and non-recurring nature.

Illegality of the business or profession does not exempt its income from tax. If it is so, all the expenses incurred in carrying on an illegal business must be allowed as deduction.

(*ii*) Compensation [Section 28(*ii*)]

Any compensation or other payment due to or received by the following persons is assessable as business income:

(*a*) any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of this management or the modification of the terms and conditions relating thereto.

(*b*) any person, by whatever name called, managing the whole or substantially the whole of the affairs of a company in India or any other company, at or in connection with the termination of the office or the modification of the terms and conditions relating thereto.

(*c*) any person, by whatever name called, holding an agency in India for any part of the activities relating to the business of any other person, at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto.

(*d*) any person for or in connection with vesting in the Government or in any corporation owned or controlled by the Government under any law for the time being in force, of the management of any property or business.

(*iii*) Income of a Trade or Professional Association [Section 28(*iii*)]

A trade association is a non-profit voluntary organisation of business competitors operating in the same line of business for the promotion of their common economic interest.

Income derived by a trade, professional or similar association from specific service performed for its members only is considered to be business income and taxed accordingly. Section 28(*iii*) further says that income arising from specific services

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rendered by the association to its members is taxed only and income not arising from specific purpose is outside the purview of this clause, *e.g.*, entrance fees or member's periodical subscription etc. are not taxable.

This provision does not apply to social clubs. Under section 44A, in case of trade association if the total amount of expenditure exceeds the receipts from the members, the deficit will be allowed as deduction in computing the income of the association assessable under the head 'Profits and Gains of Business or Profession' or in computing the income assessable under any other head. The deduction of this type is subject to the following two conditions:

(*a*) The association does not distribute its income to its members except as grants to any association or institution affiliated to it.

(*b*) The amount of deduction to be allowed should not exceed 50% of the total income of the association before this deduction.

If there is no income under that head or the deficiency exceeds such income, then the whole or balance of the deficiency can be set off against the income under any other head. However, the deficiency deductible should not exceed half of the total income of the association.

The Finance Act 1990 has inserted following three clauses u/s 28:

(*iiia*) Profit on sale of Licence

Granted under the Imports (Control) Order 1955 made under the Imports and Exports (Control) Act 1947.

It has been inserted retrospectively from 1.4.62.

(*iiib*) Cash Assistance

(By whatever name called) received or receivable by any person against exports under any scheme of the Government of India.

It has been inserted retrospectively from 1.4.67.

(*iiic*) Any Duty of Customs or Excise

Repaid or repayable as drawback to any person against exports under the Customs and Central Excise Duties Drawback Rules 1971.

It has been inserted retrospectively from 1.4.72.

(*iv*) Value of benefit or perquisite [Section 28(*iv*)]

The value of any benefit or perquisite, whether convertible into money or not arising from business or the exercise of a profession, is chargeable under the head 'Profits and Gains of Business or Profession'. As the benefit and perquisites received by an employee fall and are taxed under the head 'salaries', similarly benefits and perquisites arising from business or exercise of profession are taxed under the head 'Profits and Gains of Business or Profession'.

(*v*) Salary, Interest, Bonus, Commission or remuneration received by a partner from a firm [Section 28(*v*)]

With effect from assessment year 1993-94 any salary, interest, bonus, commission or remuneration received by a partner of a firm from firm assessed as

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firm under Income-tax Act 1961, is to be treated as business income in the hands of partner.

In case such payments are subjected to restriction u/s 40(*b*) the income under this section shall be adjusted to the extent amount is disallowed.

(*vi*) Speculation Business

Explanation No. 2 of section 28 says that where speculative transactions carried on by an assessee are of such nature as to constitute a business, such business shall be deemed to be distinct and separate from any other business.

Section 45(3) has explained a speculative transaction as "a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips.

It is clear from this that where actual delivery of goods or transfer of scrips (shares) takes place such transactions are not speculative, however highly speculative they may be in fact. Hedging business considered to be a non-speculative and such transactions are made by business to set off the effect of future price fluctuations.

The point to be noted in this connection is as to how ultimately the transaction is settled. If the difference is paid—it will be speculative and if actual delivery of the product is made then it will not be speculative.

Speculative transactions in different commodities and in different markets are to be treated as one business, distinct and separate from any other business.

The net result of speculative business is calculated. It means the loss in the speculative transaction is set off against the profits of another speculative transaction in the same previous year.

(*vii*) Profit Earned from an Illegal Business

The income earned from any business—whether legal or illegal—is taxable. Income-tax law does not make any distinction between a legal and illegal business. If an assessee earns any income from illegal business, it is computed in the ordinary manner and chargeable to tax alongwith income earned from a legal business. Thus income earned from smuggling business was held to be taxable income *[C.I.T. v. Piara Singh (1972) 83 I.T.R. 678 (Punjab)]*.

One point to be noted in this connection is that all expenses incurred to earn income from illegal business and which are incidental to such business are to be allowed as deduction out of the income earned from illegal business. Loss computed under illegal business cannot be set off against the profit of legal business. But penalties levied for infraction of law, expenses incurred in defence of criminal proceedings are, however, not allowed *[Hazi Aziz & Abdul Shakoor Bros. v. C.I.T. (1961) 41 I.T.R. 350]*.

(*viii*) Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.

Computation of Income

While computing income under the head 'Profits and Gains of Business or Profession' the following important guiding points should be kept in mind. A good

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part of Indian Income-tax Act is based upon court judgements and these principles were the basis of so many court pronouncements which are always kept in mind while computing income under this head. So some of the *principles* based on the leading cases are as follows:

(*i*) *Business carried on by the assessee.* Under section 28, the person who carried on the business is always changed. It is immaterial whether the assessee is doing the business or work himself or through some of his employees, agent, manager etc. The important point to be kept in mind is that the business should have been carried on by the assessee at any time during the previous year and not necessarily throughout the year or even in the assessment year. The assessee should have the right to carry on the business. In case a person is deprived of the right to carry on the business, the same person cannot be chargeable to tax under this head since he cannot be regarded as 'carrying on' the business.[1] Guardians for minors or receivers or trustees may be assessed under this section in respect of profit of the business carried on by them.

(*ii*) *Tax is levied on aggregated income from all business-professions carried on by the assessee during the previous year.* The net result of each business or profession carried on by the assessee is calculated separately but when tax is to be imposed, the result of all the businesses is aggregated and then whatever income comes, tax is imposed on that income. It means the loss from one business is set off against the profit of another business in this aggregation.

(*iii*) *Speculation business.* The speculation business of the assessee is kept separate. If there is profit—it will be taxed along with other business income. But if there is speculation loss—it can be set off against profits of speculation business only and not against profits of any other business.

(*iv*) *Profit on sale of assets on the winding up of a business.* The profit arising from some of the assets after winding up a business is not taxable but the profit on the sale of stock-in-trade is taxable. If the entire business is sold in one lot for a single unapportioned consideration and the assets include stock-in-trade, the profit in the sale of stock-in-trade is not separable; in such case the entire profit on sale of the business will not be taxable under this head.

(*v*) *Tax on Real owner.* It is not only the legal ownership but also the beneficial ownership that has to be considered under section 28. The income is taxable in the hands of a person to whom it actually accrues. No tax can be levied on *benamidar* in whose name the business transactions are effected and who is not really entitled to the profits.

(*vi*) Tax is levied only on the profits of the previous year. When there is expectation of profit, it cannot be taxed in anticipation. So the profit is taxed only when it has actually arisen. Further the profit must be really a gain to the person carrying on the business. Income or gain to be taxed must relate to the previous year. Each year is a self contained accounting period.

Deductions allowed—general principles

Sections 30 to 37 of Income-tax Act provide for the deductions to be allowed while computing profit under the head 'Business or Profession'. There are numerous

1. Saifuddin Ali Mohammad v. C.I.T. (1954) 25 I.T.R. 237.

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types of expenses varying from business to business and according to the nature of the unit. Under these sections, an effort was made to enlist every type of expense. But this list is not the final list; any other expenditure if at all incurred for earning a particular income, the same shall be allowed as deduction to calculate the real profit. The admissibility of an item of expenditure is governed by the following general *principles*. These are:

1. Any expenditure incurred in consideration of commercial expediency and on the basis of the principles of ordinary commercial trading is allowed as deduction.
2. Commercial expediency simply means the expenditure made by prudent man for the purpose of his business, in the best interest of his business or any other expenditure incurred totally, and exclusively for the purpose of the business.
3. Any other expenditure which was incurred in the *carrying on* of the business or profession and is incidential to such business or profession.
4. Only those expenses are allowed which are not prohibited, expressed or implied.
5. In the case of a new business, accounting year commences on the date when the business is set up. Expenditure incurred prior to setting up cannot be allowed as it falls outside the accounting year. So deductions are made regarding those expenses only which are incurred in the relevant accounting year. Each accounting year is separate and distinct one.
6. Deduction is to be made from the business for which the expenses were made. In case of more than one business, the expenses of one cannot be charged from the other in any case.
7. The expenditure of a business which was discontinued before the commencement of the accounting year cannot be charged from the existing business. A general rule in such cases is that the expenses of a dead business become capital loss.
8. In case of a single transaction all expenses are allowed whether incurred in that accounting year or earlier to that.
9. A partner is allowed a deduction from his share of income from the firm's profit such expenses which he might have incurred in earning this partnership profit.
10. Only expenses are allowed to be deducted while the loss of any type is not allowed without considering its nature.
11. Capital expenditure is not allowed.
12. Expenditure which is deductible for income-tax purposes is one which is towards a liability actually existing at the time but putting aside a money which may become expenditure on the happening of an event is not expenditure.
13. Deduction will be allowed in case of only those expenses which have been incurred for the purposes of the assessee's *own* business.

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14. Any amount previously allowed as deduction, if the same is recovered, will be taxable in the year in which it is so recovered.
15. The onus of proof that a particular expenditure is permissible as a deduction falls upon the assessee.

Deductions

Section 29 says that the profits under the head 'Profits and Gains of Business or Profession' are calculated in accordance with the provisions contained in sections 30 to 44A, which provide for the deductions to be made from the gross income. These deductions are:

	Section
1. Rent, rates, taxes, repairs and insurance for building, used for the purpose of the assessee's business	30
2. Repairs and insurance premium paid in connection with the plant, machinery, furniture etc. used in business or profession	31
3. Depreciation of buildings, machinery, plant or furniture	32
4. Tea Development Account and Reserve for Shipping companies —*Explained in next chapter*	33AB and 33AC
5. Expenditure on scientific research	35
6. Expenditure on patents and copyrights	35A
7. Expenditure on know-how	35AB
8. Expenditure on eligible projects or Schemes	35AC
9. Expenditure by way of payment to associations and institutions carrying out Rural Development Programme	35CCA & 35CCB
10. Amortisation of certain preliminary expenses	35D
11. Deduction for expenditure on prospecting, etc. for certain minerals	35E
12. *Other Deductions*	36
Insurance premium of Stock-in-trade	
Bonus or commission to employees	
Interest on borrowed capital	
Employer's contribution to provident and other funds	
Employer's contribution to the approved gratuity funds	
Loss of animals	
Bad debts	
Transfer of money to special reserve in case of financial institutions only	
Expenditure incurred on family planning case of companies only	
13. *General*	37
Any other type of expenses incurred but not covered under sections 30 to 36	
14. Buildings partly used for business premises	38

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15.	Expenses expressly disallowed while computing income under business or profession	40
16.	Expenses not allowed to be deducted under certain circumstances	40A
17.	Deemed profits	41
18.	Deductions in case of oil mining concerns	42
19.	Definitions of certain terms	43
20.	Certain deductions to be allowed only on actual payments	43B
21.	Insurance Business Profits	44
22.	Maintenance of Accounts by certain Professionals	44AA & 44AB

EXPRESSLY ADMISSIBLE DEDUCTIONS (Section 30—35)

Rent, Rates, Taxes, Repairs and Insurance in the case of Building Premises (Section 30)

A deduction is allowed regarding rent, rates, taxes, repairs and insurance premium paid for the building premises where the assessee is carrying on his own business or profession.

(*a*) Rent

(*i*) The full amount of rent will be an admissible deduction in case the building premises are taken on rent.

(*ii*) In case no rent is paid or the assessee owns the business premises, then no deduction shall be allowed because the landlord cannot be a tenant also. If it is so, the assessee will not be taxed for the building income under the head 'House Property'.

(*iii*) If business premises belong to one of the partners of the firm, the rent paid to the landlord-partner shall be an admissible expense of the firm's business or profession.

(*b*) Repairs

(*i*) In case the assessee is a tenant, and the agreement of rent provides that the tenant will bear the cost of repairs; the amount paid or spent on account of such repairs, is allowed as deduction.

(*ii*) Otherwise than as a tenant, *e.g.*, the assessee is the owner of the premises, the amount which the assessee spends on repairs will again be allowed as deduction.

The word 'repairs' here mean such repairs which are required to keep the building in the workable condition *i.e.*, minor changes (replacements) due to wear and tear. Repairs are simply to keep the asset working. It should not result into any increase in the value, efficiency etc. of the asset.

(*c*) Local Taxes, etc.

Any sums paid on account of land revenue, local rates or municipal taxes in respect of the premises used for the assessee's business, if the assessee is the owner

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of the building, are allowed under this category. In case the building is on rent then such part of these expenses which the assessee is supposed to pay under the contract of rent entered between the landlord and assessee are also allowed.

(*d*) Insurance Premium

The amount of any premium paid in respect of insurance against risk of damage or destruction on the premises of the assessee used for his business or profession is allowed as expenditure. Insurance may be against fire, earthquake etc.

Where the assessee has sub-let a part of the premises, the deduction under Section 30 will be limited to the difference between the rent paid and the rent received from sub-letting. Section 38(i) deals with the cases where the part of the house is used for business purpose and the remaining part for residence of the assessee. In such cases the deduction will be limited to that part of the building which is used for the business purposes.

Repairs and Insurance of Machinery, Plant and Furniture (Section 31)

Under Section 31, the following deductions shall be allowed in respect of repairs and insurance of machinery, plant and furniture used for the purposes of the business or profession:

(*i*) The amount paid on account of current repairs thereto;

(*ii*) The amount of any premium paid in respect of insurance against the risk of damage or destruction thereto.

The plant, machinery, furniture etc. on which this deduction is to be claimed must be used for the business of the assessee. The repairs must be in the ordinary course to replace or to compensate the wear and tear of the asset, *i.e.*, to keep the asset in the working order only and these should not be of capital nature.

Depreciation on Fixed Assets (Section 32)

Depreciation on the fixed assets is very important item of deduction of any business. This is dealt at length in a separate chapter.

Expenditure Incurred in the Field of Scientific Research (Section 35)

Section 43(4) defines the scientific research as activities for the extension of knowledge in the fields of natural or applied science including agriculture, animal husbandry or fisheries.

References to expenditure incurred on scientific research include all expenditure incurred for the prosecution, or the provision of facilities for perusing the scientific research, but does not include any expenditure incurred on the acquisition of rights in or arising out of scientific research. References to scientific research related to a business or class of business include:

(*a*) any scientific research which may lead to or facilitate an extension of that business or, as the case may be, all business of that class;

(*b*) any scientific research of a medical nature and which has a special relation to the welfare of workers employed in that business or, as the case may be, all businesses of that class.

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Section 35 lays down while computing the income of that business or profession, the following deductions shall be allowed in respect of expenditure on scientific research. The expenses are of two types:

1. Revenue expenditure, 2. Capital expenditure.

Revenue Expenditure [35(1)]

(*i*) Any expenditure (of revenue nature) incurred or expended on scientific research related to the business of the assessee. This expenditure must be incurred by the assessee himself. Any salary paid to personnel engaged in scientific research and purchase of materials used in such scientific research during the period of 3 years immediately preceding the commencement of the business will be *deemed to have been expended in the previous year in which business is commenced.* The deduction will be allowed only if the expenditure has been incurred after 31.3.73 on research related to assessee's business and will be limited to the extent of amount allowed by prescribed authority.

(*ii*) Any sum paid to an approved scientific research association or to an approved University, college or to a public sector company institution to be used for scientific research related to the assessee's business.

(*iii*) Any sum paid to a university, college or other institution to be used for research in social science or statistical research carried on by a university, college or institution which is for the time being approved for the purpose of this clause by the prescribed authority by notification in Official Gazette.

With effect from 1.4.90 relevant to Assessment year 1990-91 following restrictions have been imposed by the Direct Tax Laws (Amendment) Act 1989:

(*i*) The concerned institutions must be approved by the prescribed authority on an application made in the prescribed form;

(*ii*) The prescribed authority can call for such documents including audited accounts as are required to satisfy itself about genuineness of the activities of such institution;

(*iii*) No such institution will be notified for a period more than 3 years at a time.

Deduction when amount is paid to an Approved Institution [Section 33(2A)]

With effect from 1.4.1984 only that sum shall be allowed which is paid with specific direction that the sum paid shall not be used for the acquisition of any land or building or construction of any building.

Weighted deduction when amount is paid to a National Laboratory [Section 35(2AA)]

With effect from assessment year 1994-95 an assessee can claim a deduction of 125% of actual amount given to a National Laboratory to be used for scientific research undertaken under a programme approved by the prescribed authority. No deduction in respect of such amount shall be allowed under any other provision of the Income-tax Act.

The term 'National Laboratory", means a scientfic laboratory functioning at the national level under the aegis of the Indian Council of Agricultural Research, the

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Indian Council of Medical Research or the Council of Scientific and Industrial Research and which is approved as National Laboratory.

The Finance Act 1994 has extended this benefit for any amount given to any University or Indian Institute of Technology and it shall also qualify for weighted deduction.

While granting the status of National Laboratory the prescribed authority shall satisfy itself about the feasibility of carrying on the research and shall submit its report to the Director General in prescribed form.

Capital expenditure scientific research

With effect from 1.4.67 capital expenditure incurred on scientific research is fully allowed to be dibited in the year in which it is incurred subject to following :

Capital expenditure on acquisition of land

No deduction shall be admissible in respect of any expenditure incurred on the acquisition of land whether the land is acquired as such or as part of any property after 29th day of Feb. 1984.

In the explanation given in this section it is said that where any capital expenditure has been incurred before the commencement of business, such expenditure incurred in three years immediately preceding the commencement of the business shall be deemed to have been incurred in the previous year in which the business is commenced.

If, in any year the profits are insufficient to absorb the full amount of capital expenditure on scientific research, unabsorbed part of such expenditure can be carried forward for indefinite period like unabsorbed depreciation and can be set off against the income of any head in future years [Section 35(4)]. Assets representing capital expenditure on scientific research are not eligible for depreciation.

In case such a capital asset is transferred, the sale price to the extent it is equal to the amount of deduction allowed is treated as the taxable income of the business of that previous year in which the sale takes place and in case where the sale price is in excess of that deduction allowed such an excess is treated as the capital gain of the year.

Prescribed authority for scientific research. According to Rule 6, for the purpose of section 35, the "prescribed authority" shall be:

(*i*) in relation to research in the fields of agriculture animal husbandry and fisheries, the Indian Council of Agricultural Research;

(*ii*) in relation to research in the field of medical science, the Indian Council of Medical Research;

(*iii*) in relation to research in the field of social sciences or statistical research, the Indian Council of Social Science Research; and

(*iv*) in relation to research in the field of other natural or applied science, the Secretary, Department of Science and Technology (Government of India or any other officer of the Department nominated by it in this behalf).

Illustration 1. Discuss the admissibility of following items :

(*i*) Amount spent on acquisition of land for setting up research laboratory Rs. 2,00,000.

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(*ii*) Expenditure on construction of building for such laboratory— Rs. 3,50,000.

(*iii*) Amount of salary paid to staff engaged in research.
(*a*) Rs. 60,000 paid before 1-4-96 *i.e.* date of commencement of business. Research was relating to assessee's own field of business.
(*b*) Rs. 42,000 paid of the 1-4-96 as salary to staff engaged in such research.

(*iv*) A computer costing Rs. 1,60,000 was purchased with the object of using it for research but on acquisition it was found that it can't be used for research. Nevertheless it was installed in the business office.

Solution

(*i*) Expenditure incurred to acquire land for research is disallowed u/s 35 (2).

(*ii*) Capital expenditure incurred on construction of building *i.e.* Rs. 3,50,000 is fully allowed u/s 35 (2). In case any amount remains unadjusted it can be carried forward till fully adjusted from gross total income.

(*iii*) (*a*) Rs. 60,000 paid as salary to staff engaged in research is fully allowed during previous year 1996-97. u/s 35 (1) any expenditure incurred during 3 years prior to year of commencement is deemed to have been spent in the year in which business commences, provided research relates to assessee's own field of business.

(*b*) Salary of Rs. 42,000 paid during 1996-97 is fully allowed u/s 35 (1).

(*iv*) The cost of computer can be debited as capital expenditure on research. But it will be treated as business asset as it was not used for research and will qualify for depreciation u/s 32.

Q. No. 1.

Calculate taxable profit of the assessee for the assessment year 1997-98 from the particulars given below :

	Rs.
Profit for the previous year 1996-97 (Before charging the following amounts)	2,60,000
(*i*) Amount given to National Laboratory (so notified)	20,000
(*ii*) Cost of land acquired for constructing research laboratory	1,00,000
(*iii*) Cost of Building and P & M required for research	3,50,000
(*iv*) Amount given as salary to staff engaged in research (relating to a field not related to assessee's own business) during 1995-96 (Business started on 1-4-96)	30,000
(*v*) Salary given to staff engaged in research within the premises during 1996-97	60,000

[Hints: (*i*) Rs. 25,000 to be allowed (*ii*) and (*iv*) Not allowed (*v*) allowed (*iii*) Adjusted upto Rs. 1,75,000 to be C/F 1,75,000.

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Deduction for Expenditure on a Programme Undertaken by Assessee [Section 32(2B)]

With effect from 1.3.1984, where an assessee has incurred any expenditure (not being in the nature of capital expenditure incurred on the acquisition of any land or building or construction of any building) on scientific research undertaken, he shall be allowed a deduction of a sum equal to actual expenditure.

Capital expenditure on Research for prescribed things [Section 35(2AB)]

1. In case any capital expenditure (not being expenditure on land and building) is incurred by **company** engaged in the manufacture or production of drugs, pharmaceuticals, electronic equipments, computers, telecommunication equipments, chemicals or any other article or thing notified by the Board, on scientific research and development facility as is approved by the prescribed authority, a deduction of 125% of such expenditure shall be allowed.

2. In case any deduction is allowed under this section no deduction under any other section can be claimed for such expenditure.

3. This deduction shall be allowed only if the company has entered into an agreement with the prescribed authority for co-operation in such research and development facility and for the audit of the accounts maintained for that facility.

4. The prescribed authority shall send its report in relation to approval of the said facility to the Director General in prescribed form.

This amendment shall come into effect from assessment year 1998-99.

Expenditure incurred on the acquisition of Patents Rights or Copy Rights (Section 35A)

Sometimes the assessee has to purchase these rights, and as the benefits of these rights is spread over a number of years, similarly the expenditure on the acquisition of these rights (after 28 Feb. 1966) is also spread over and is claimed over a number of years. Whole expenditure is divided into fourteen equal instalments and every year one instalment is allowed as deduction beginning with the previous year in which such expenditure is incurred. In certain cases the expenditure is incurred before the commencement of the business, the fourteen previous years are counted beginning with the previous year in which the business commences.

In case these rights are acquired in a previous year prior to previous year in which such expenditure is incurred, the deduction in such case will be spread over in as many instalments as are left out of 14 after deduction of the complete years that have elapsed after the commencement of 'right'. Where the period of 14 years have elapsed since the acquisition of the right, the full capital expenditure shall be allowed in one instalment only in the year in which expenditure is incurred.

For example, the assessee purchased a copyright for Rs. 14,000 in the year 1996-97. A deduction of Rs. 1,000 for 14 years will be allowed beginning from the previous year 1996-97. Supposing the right is acquired in the year 1996-97 but the payment for the same was made after the lapse of 7 years, the expenditure will be divided in seven instalments and a deduction of Rs. 2,000 for 7 years will be allowed.

If the rights come to an end or are sold and sale proceeds are less than the cost of acquisition thereof not charged, so far, a deduction equal to such cost remaining

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is allowed or, as the case may be, such cost remaining unallowed as reduced by the proceeds of the sale shall be allowed in respect of the previous year in which the rights come to an end, or as the case may be, are sold.

If sale proceeds are more than the cost of acquisition remaining unallowed, the excess part will be business income of the previous year in which, the whole or any part of the rights is sold. In case of loss on account of sale of part of such rights, the loss will be spread over remaining number of years. The excess of amount realised over *actual cost* shall be capital gain.

Explanation. Where the whole or any part of the rights is sold in a previous year in which the business is no longer in existence the provisions of this sub-section shall apply as if the business is in existence in that previous year.

Illustration 2. A businessman entered into agreement with a collaborator for purchase of patent right on 1-6-94. How much amount can be debited to P & L A/c during the previous year 1996-97 if

(*a*) price of Rs. 14 lacs was paid at the time of agreement or ;

(*b*) price is paid in 1996-97; or

(*c*) price is still to be paid during 1999-2000.

Solution

(*a*) u/s 35A the cost of patent right can be written off in 14 equal instalments commencing with the year in which business commences. In this case Rs. 1,00,000 can be debited to P & L A/c during the previous year 1996-97.

(*b*) As price is paid 2 years (94-95 and 95-96) after its use, $^{1}/_{12}$th of Rs. 14,00,000 *i.e.* 1,16,667 can be debited to P & L A/c during the previous year 1996-97.

(*c*) As price is still to be paid hence nothing can be debited to P&L A/c during the previous year 1996-97.

Q. No. 2

Calculate the various claims/incomes for the previous year 1996-97.

(*a*) Cost of patent right purchased in 92-93 for Rs. 7,00,000 but used with effect from 1-6-95 *i.e.* day of commence-ment of business.

(*b*) A copyright purchased and used with effect from 93-94 but price of Rs. 1,10,000 is paid in 1996-97.

(*c*) A copy right was purchased and used with effect from 88-89 for Rs. 2,80,000 and every year Rs. 20,000 have been debited.

It is sold during 1996-97 for

(*i*) Rs. 1,00,000 or (*ii*) Rs. 2,00,000 or (*iii*) Rs. 3,00,000.

[Hints : (*a*) Rs. 50,000 to be debited (*b*) 1/11th *i.e.* Rs. 10,000 to be debited (*c*) (*i*) Rs. 20,000 to be debited (*ii*) Deemed Profit Rs. 80,000 (*iii*) Deemed Profit Rs. 1,60,000 and capital gain Rs. 20,000]

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Expenditure on know-how (Section 35 AB)

(*a*) When technical know-how is acquired in any previous year the lump-sum consideration paid shall be allowed to be deducted in six equal instalments commencing from the previous year in which such consideration is paid.

(*b*) In case technical know-how acquired was developed in any Indian laboratory, university or institution referred under section 32A, the consideration paid shall be written off in three equal instalments.

Expenditure for obtaining licence to operate telecommunication services [Section 35 ABB]

With effect from assessment year 1998-99 this new subsection is being introduced.

1. In case any capital expenditure is incurred for acquiring a license to operate telecommunication services and actual payment has been made, a deduction of an amount equal to appropriate fraction shall be allowed in every previous year during which the license shall be in force.

   Appropriate fraction = actual payment made X 1/ Number of previous years for which the fee is paid.

   "Actual payment has been made" means the actual payment of expenditure irrespective of the previous year in which liability for the expenditure was incurred according to the method of accounting regularly employed by the assessee.

2. In case the licence is sold and capital sum realised from transfer is less than the expenditure remaining unallowed shall be fully allowed to be debited in the year in which it is sold.

3. In case the capital sum realised is more than the amount of expenditure remaining unallowed, the differance between the money realised and amount remaining unallowed shall be chargeable to tax as income under the head Profits and gain of business and profession in the previous year in which license is transferred but it shall not exceed the amount which has been written off so far. In case the license is transferred in the year in which business is not in existance, even than this provision shall be applicable as if business is in existance.

4. In case licence is transferred wholly or in part and capital sum realised is not less than the expenditure incurred remaining unallowed, no deduction for such expenditure shall be allowed in the year in which such licence is transferred and in any subsequent previous year.

5. In case any part of the licence is sold and money realised is more than the unallowed amount and the excess amount does not exceed the amount allowed so far, such excess shall be taxable as business profit. In case the amount realised does not exceed the unallowed value, the differance can be written off in remaining number of years.

Expenditure on eligible projects or schemes [Section 35 AC]

(*i*) This deduction has come into force from 1.4.92, *i.e.*, assessment year 1992-93.

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(*ii*) It is allowed to all assessees.

(*iii*) Rate of deduction is 100% of amount actually given during the previous year.

(*iv*) The amount is to be given to a—

(*a*) Public Sector Company; or

(*b*) Local authority; or

(*c*) An institution; or

(*d*) An association; which is approved by the National Committee constituted by the Central Government.

(*v*) The company assesses may claim this deduction by incurring such expenditure either by way of payment to above noted persons or directly on the eligible project.

(*vi*) When a person, other than company claims this deduction, it must furnish a certificate from the company, institution, local authority or the association, as the case may be, alongwith return as proof of payment.

(*vii*) In case of company assessees this deduction is to be allowed only on production of proof of payment. In case expenses are incurred by company directly it must submit a certificate from Chartered Accountant in the prescribed form [35AC(2)].

(*viii*) In case a deduction is claimed by a person under this section it cannot be claimed under any other section [35AC(3)].

The approval granted by the National Committee can be withdrawn if the Commitee is not satisfied about the proper execution of project but after giving a reasonable opportunity of show cause against the proposed withdrawl. [Section 35AC (4) and (5)]

Contribution to an association carrying out any programme of rural development

[Section 35 CCA]

The Finance Act 1978 inserted this section which provides for deduction for any expenditure incurred during the previous year by *any assessee* by way of payment of any amount

(*a*) to an institution or association which has its object the undertaking of any programme of rural development, to be used for carrying out any programme of rural development approved by the prescribed authority ; or

(*b*) to an institution or association which has its object the training of persons for implementing the above mentioned programmes ; or

(*c*) to a rural development fund set up and notified by the Central Government, or

(*d*) to the National Urban Poverty Eradication Fund set up and notified by the Central Government.

This provision has come into effect from 1.6.1978, which means expenditure incurred under this provision after 31.5.78 shall qualify for deduction.

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This benefit will be available only if certain conditions (as have been prescribed in Section 35 CC with effect from assessment year 1984-85) are satisfied by the assessee.

Conditions

Deduction under this section shall be allowed only if following conditions are also satisfied:

(*i*) The assessee has obtained the approval of the prescribed authority in respect of such programme before the 1st day of March 1983;

(*ii*) Such programme involves work by way of construction of any building or other structure whether for use as dispensary, school, training or welfare centre, workshop or any other purpose or the laying of any road or the construction or boring of a well or tubewell or the installation of any plant and machinery and such work has commenced before the 1st day of March 1983;

(*iii*) The expenditure on such programme is incurred in a case where the approval of the prescribed authority in respect of such programme has been granted for a specified period before the expiry of that period and any other case before the 1st day of March 1984;

(*iv*) The assessee furnishes, alongwith the return of income for the assessment year for which the deduction is claimed, a statement of such expenditure in the prescribed form duly signed and verified by Chartered Accountant; and setting forth such particulars as may be prescribed.

The Finance Act 1979 has clarified that this benefit will be available only if contribution is made to an association or institution which is approved in this behalf by prescribed authority.

This deduction will also be available on any amount paid to a rural development fund set up and notified by the Central Government in this behalf.

Contribution to an association carrying out any programme of conservation of natural resources [Section 35 CCB]

In case an assessee incurs any expenditure by way of payment of any sum—

(*a*) to an institution whose object is undertaking of any programme of conservation of natural resources or afforestation, to use such amount for carrying out any programme of conservation of natural resources or afforestation which is approved by prescribed authority; or

(*b*) to such fund for afforestation as may be notified by the Central Government;

The amount so given is allowed to be debited to Profit & Loss Account of the year.

In case an assessee has claimed deduction of any amount under this section, he cannot claim deduction for such expenditure under any other section of the Act.

This amendment has come into effect from 1st June 1982, *i.e.*, assessment year 1983-84.

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Amortisation of Certain Preliminary Expenses (Section 35D)

Under Section 35D, the deduction is allowed only in case of an Indian company or a person (other than company) resident in India. The deduction is in respect of the expenditure incurred after 31st March 1970 and expenditure may be of the type which was incurred—

(*i*) before the commencement of the business, or

(*ii*) after the commencement of the business, or in connection with the extension of its industrial undertaking or in connection with its setting up a new industrial unit.

The following expenses shall be eligible for deduction under Section 35D (2).

(*a*) Expenditure in connection with:

(*i*) preparation of feasibility report;

(*ii*) preparation of project report;

(*iii*) conducting market survey or any other survey necessary for the business of the assessee;

(*iv*) engineering services related to the business of the assessee;

(*b*) Legal charges for drafting any agreement between the assessee and any other person for any purpose relating to the setting up or conduct of the business of the assessee:

(*c*) The following expenses in case of company assessees:

(*i*) legal charges for drafting the Memorandum and Articles of Association of the company;

(*ii*) expenses incurred on the printing of Memorandum and Articles of Association;

(*iii*) by way of fees for registering the company under Companies Act, 1956;

(*iv*) in connection with the Issue, for public subscription of shares, and debentures of the company, being underwriting commission, brokerage and charges of drafting, for typing, printing and advertisement of the prospectus.

(*d*) Such other items of expenditure (not being expenditure eligible for any allowance or deduction under any other provision of this Act) as may be prescribed.

The above-mentioned expenditure is divided into *TEN* instalments and the assessee shall be allowed a deduction of an amount equal to one instalment (1/10) for each of the ten successive previous years beginning with the previous year in which business commences or extension work is completed or the new industrial unit commences production as the case may be.

The maximum amount eligible for deduction as preliminary expenses shall not exceed 2.5% of the 'Cost of project' or in case of company assessee at the option of the company, the amount of deduction will be the amount, equal to 2.5% of 'Capital employed in the business of the company'.

Expenditure on Prospecting etc., for certain Minerals [Section 35E]

Where an assessee, being an Indian company or a person (other than a company) who is resident in India, is engaged in any operation relating to prospecting for,

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extraction or production of any mineral and incurs, after 31st day of March 1970, any expenditure specified below, the assessee shall, in accordance with and subject to the provisions of this section, be allowed for each of the relevant previous years a deduction of an amount equal to one-tenth (1/10) of the amount of such expenditure.

This expenditure refers to the expenditure incurred on the prospecting for any mineral (specified in schedule VII of the I.T. Act) or on the development of mines or other natural deposits of any such mineral; but does not include;

(*i*) Expenses incurred on the acquisition of the site of the source of any mineral or group of associated minerals in question;

(*ii*) Expenses incurred on the acquisition of the deposits of the minerals referred to above;

(*iii*) Expenses of capital nature incurred in respect of any building, machinery, plant or furniture (such assets on which depreciation is allowed under section 32).

The expenditure on which deduction is to be allowed should have been incurred after 31st March 1970 and at any time during the year commercial production is started and any one or more of the four years immediately preceding that year.

If, in any year, the profits are insufficient to absorb the full amount of the instalment, the amount of the instalment up to available profits will be allowed and the balance *will be carried forward* and *added in next previous year's instalment and so on for succeeding previous year, but no part of any instalment can be carried forward beyond the tenth previous year.*

In arriving at the amount of expenditure, the amount met by any third party, and any sale, salvage compensation of insurance moneys received by the assessee, are to be deducted from the expenditure.

Audit

In case of non-corporate assessees deduction under section 35D and 35E will be allowed only if the accounts of the concern are duly audited by a Chartered Accountant or a person eligible under Companies Act.

OTHER DEDUCTIONS (Section 36)

While computing the income of a business or profession, other expenses in the nature of following are admissible:

(*i*) *Insurance Premium.* The amount of any insurance premium paid in respect of insurance against risk of damage or destruction of stocks or stores used for the purpose of the business or profession.

(*ia*) *Insurance Premium for Cattle.* The Finance Act 1979 has introduced new sub-section (*ia*) under which any premium paid by a Federal Milk Co-operative Society to effect or to keep in force an insurance on the life of the cattle owned by a member of a co-operative society being a primary society engaged in supplying milk raised by its members to such federal milk co-operative society is allowed.

(*ib*) *Insurance Premium for Employees.* The amount of any premium paid *by cheque* by the assessee as an employer to effect or to keep in force an insurance on

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the health of his employees under a scheme framed in this behalf by the General Insurance Corporation of India and approved by the Central Government.

(*ii*) *Bonus or Commission.* Any sum paid to an employees in addition to salary or bonus or commission for services rendered, where such sum would not have been payable to him as profits or dividend if it has not been paid as bonus or commission.

The amount of bonus or commission paid should be reasonable with reference to:

(*a*) the pay of the employee and conditions of his service;

(*b*) the profit of the business or profession for the previous year in question; and

(*c*) the general practice or local practice in similar business or profession.

The point to be noted in this case is that the undertaking should not pay bonus or commission with a view to reduce the taxable profits. This is quite possible in private companies and specially where the shareholders are the employees of the company.

Bonus paid as a result of industrial dispute, is an allowable deduction under section 37 and not under section 36.

In factories where the Payment of Bonus Act 1965 is applicable the deduction regarding bonus being a statutory liability shall be equal to the bonus payable under this Act.

(*iii*) *Interest on Borrowed Capital.* Any interest paid on borrowed capital is an allowable deduction. The borrowed capital must be used in the business/profession of the assessee. The borrowing must, however, be genuine and not bogus and the assessee must have paid as interest the amount claimed as deduction under this category.

Allahabad High Court has held in a case *[Banarsi Dass Gupta v. C.I.T. (1977) Tax I.R. 65]* that in case interest paid is not on genuine or is on illusory borrowings made for assessee's business, any interest paid on such borrowings shall not be allowed as deduction.

The Income-tax department cannot disallow this item on the ground that borrowing of money was not required and the rate of interest could be scaled down. The borrowed money may be used in the acquiring of capital assets or stock-in-trade or expansion of the business. It is essential that the money should have been utilised in the assessee's business or profession.

If the money is borrowed for the purpose of a business which is not at all assessable under the Act, no deduction can be claimed under this clause. Deduction on borrowed money will not be allowed if the borrowing was for the purposes of a business discontinued before the commencement of the accounting year.

Interest liable to tax but payable outside India, will not be allowed as deduction unless tax has been deducted at source from such interest and in respect of which there is no person in India, who may be treated as an agent. It means interest paid to a non-resident shall be allowable as deduction if tax on such interest is paid or deducted at source or there is a person in India who can be treated as an agent of such a non-resident person.

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In case interest is paid to a person outside India without deductions of tax, full such interest is disallowed. But, if, in a subsequent year tax is paid on such interest, assessee can claim deduction of interest disallowed earlier. (Inserted by Finance Act 1988 with effect from assessment year 1989-90).

In the explanation given in this clause of section 36, it is said that recurring subscriptions paid periodically by shareholders or subscribers in Mutual Benefit Societies which fulfil such conditions as may be prescribed, shall be deemed as borrowed capital within the meaning of this clause.

Interest on delayed payments under "The Interest on Delayed payment to Small Scale and Ancillary Industrial Undertaking Act, 1993"

(*i*) In case supplier supplies any goods or services to any buyer, the buyer must make the payment within stipulated time.

(*ii*) In case payment is not made in this stipulated time, the buyer shall pay interest @ 5% above the highest of the minimum lending rates charged by scheduled banks.

(*iii*) This interest will not be allowed to be debited to the P & L A/c with effect from assessment year 1993-94.

[Circular No. 671 Dated 30.9.93]

(*iv*) (*a*) *Contribution to Provident and Superannuation Fund.* Any sum paid by the assessee as an employer by way of contribution towards a recognised provident fund or an approved superannuation fund, subject to such limits as may be prescribed, is allowed as deduction.

(*v*) *Contribution to Gratuity Fund.* Any amount paid by the assessee employer by way of contribution towards an approved gratuity fund created by him for the exclusive benefit of employees under an irrevocable trust is allowed. This is subject to the provision of section 40 A (7) which is explained at a later stage in this chapter.

(*va*) *Employee's contribution to Funds.* By amending section 2 (24), a new sub-clause (x) has been introduced. Under this sub-section any amount received by employer from his employees as their contribution to any provident fund, or superannuation fund, or any fund set up under E.S.I. Act 1948 or any other fund for the welfare of such employees shall be treated as income of the assessee and shall be credited to P & L A/c of the year.

Assessee can debit to his P & L A/c such contribution of employees towards provident fund, superannuation fund, E.S.I. fund or other fund created for welfare of employees.

This deduction will be allowed only if such amount is credited to the employee's account in relevant fund on or before due date.

Due date means the date by which assessee is required to credit such contribution in the relevant fund as prescribed under respective fund.

(*vi*) *Loss of Animals.* If the animals are used in the business or profession of the assessee otherwise than as stock-in-trade and have died or become permanently useless for such purposes and any loss, suffered due to the death or becoming permanently useless for the unit, will be allowed as deduction.

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(*vii*) *Bad debts.* A deduction is allowed in respect of the debt of the business or profession which have actually become irrecoverable in the previous year. The loans advanced by banking or money-lending concerns if they are irrecoverable in full or part thereof, a deduction is allowed. The eligibility of the deduction depends upon the existence of debt which is irrecoverable under law or through the help of courts.

The following conditions are laid down in the Act u/s 36(2) which are to be fulfilled before any allowance regarding bad debts is allowed:

(*a*) The debt or loan should be in respect of business or profession of the assessee and relates to the relevant accounting year. Any debt which is not incidental to assessee's business or profession, no deduction is allowed in case of such a debt. It has been held in a case *[Girdhari Lal Gianchand v. C.I.T. (1917) 79 I.T.R. 561 (Allahabad)]* that a debt due from retired partners if it has become irrecoverable cannot be written off and claimed as deduction since it is a capital loss.

(*b*) The deduction shall be allowed in respect of only those debts which have been taken into account in computing the income of the assessee of the previous year or of an earlier previous year or should represent money lent in the ordinary course of the business of banking or money-lending.

(*c*) The debt or loan or part thereof, a deduction about which is claimed as bad debts, must have become actually bad in the accounting year.

The point simply demands that so long as there is a hope of recovering the debt, it cannot be treated as bad debt and so no deduction can be allowed. Deduction is allowed in case of only those debts which have become irrecoverable in the previous year. Any debt which has some possibility of recovery and till this possibility persists, the debt cannot be said to have become irrecoverable *[C.I.T. v. Sankara Ayyar (1951) 20 I.T.R. 597 (S.C.)]*.

(*d*) The deduction will be allowed in respect of only those bad debts which have been written off in the books of accounts of the assessee in the previous year in which the deduction is so claimed.

Bad debts of a discontinued business. Bad debt of a business which has been discontinued before the commencement of the accounting year, cannot be claimed as deduction from the profit of the continuing business of the assessee.

U/s 36(2)(*iii*) if bad debt already written off in the books of accounts but actually not allowed as deduction by A.O. on the ground that the debt has still the possibility of recovery, any such debt or part thereof shall be allowed as deduction in the year in which it actually becomes irrecoverable.

U/s 36(2)(*iv*) where any such debt or part of debts is written off as irrecoverable in the accounts of the previous year and the Assessing Officer is satisfied that such debt or part has become a bad debt in any earlier previous year not falling beyond a period of which previous years immediately preceding the previous year in which such debt or part is written off, the provisions of sub-section (6) of section 155 shall apply. It means that the assessment made for these years shall be re-opened and total income shall be recomputed after allowing the claim for bad debts.

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Bad debts Recovered. [Section 41(4)]. If in any previous year, the debt becoming bad is written off and a deduction was claimed but if later on the same debt is recovered in full or in part thereof, the amount so recovered will be treated as the income of the year in which it is received or recovered.

In another case where a part of debt was written off or allowed by the Assessing Officer as bad debt and the remaining portion was left as recoverable and if some money is received from the debtor, the amount received up to the recoverable part will be treated as normal realisation of debt. If in the final adjustment, the amount recovered is less than the amount presumed to be recoverable, the deficiency will be allowed as deduction in that previous year. If, on the other hand, the money received is more than the recoverable amount, the excess will be treated as the income of the year of receipt of such money.

Bad debts Recovered but disallowed earlier. If in any previous year, the debt written of as bad was disallowed by the Assessing Officer and later on the debt in full or in part is realised, the amount so realised shall not be treated as income in the year of realisation because the amount recovered was taxed when it was disallowed as bad debt by the Assessing Officer.

(viia) Bad debts of Banks, financial constitution and industrial investment corporation etc.

(*a*) A scheduled bank or a non-scheduled bank can create a reserve of 5% of total income (*i.e.*, before allowing deduction under this section and u/s 80) and *10%* of aggregate average advances made by the rural branches of such bank.

(*b*) A foreign bank can create reserve upto a maximum of 5% of gross total income (before allowing this deduction).

(*c*) A public financial institution, or a State financial corporation or state industrial investment corporation may create reserve upto a maximum of 5% of gross total income (before allowing this deduction).

(*viii*) *Special Reserve Created by Financial Corporation.* No deduction is allowed for creating such reserves. But in case of financial corporations or, as the case may be, public company engaged in providing long-term finances for industrial and agricultural development in India and approved by the Central Government for the above mentioned purpose such deduction is allowed at the following rates:

(*a*) In respect of any special reserve created by a financial corporation which is engaged in providing long-term finance for industrial or agricultural development in India or by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes, an amount not exceeding 40% of the total income (computed before making any deduction under this clause) can be carried to such reserve account.

(*b*) In respect of special reserve created by a financial corporation which is engaged in providing long term industrial or agricultural development or development of infrastructure facility in India or by a public company formed and registered in India with the main object of carrying on the

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bussiness of providing long term finance for construction or purchase of houses in India for residential purposes, an amount not exceeding 40% of the profits derived from such business of providing long term finance (computed under the head Profits and Gains of Business or Profession before making any deduction under this section) can be carried to such reserve account.

(*c*) In the case of any other financial corporation—25% of the total income.

Total income for this purpose means income computed before allowing this deduction.

For the above purpose *'long term industrial finance'* means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment alongwith interest thereof during a period not less than 5 years.

With effect from 1.4.1982 the aggregate of amounts carried to such reserve should not exceed twice the amount of paid-up capital and general reserves.

(*viiia*) *Special reserve created by a scheduled bank (other than Foreign banks).* If such bank is engaged in banking operations outside India, will be entitled to a deduction, in computation of their taxable income, upto 40% of the total income carried, by them to special reserve account provided the scheduled bank is approved by the Government. The amendment has taken effect from 1st April 1983 *i.e.*, assessment year 1983-84.

(*ix*) *Expenditure on Family Planning.* The company assessees are allowed a deduction in respect of the *bona fide* revenue expenditure incurred by them for the purpose of promoting family planning amongst its employees.

In case where capital expenditure is incurred for family planning purposes, the expenditure will be spread over a period of five years and every year one instalment will be allowed as deduction beginning from the previous year in which expenditure was incurred.

(*x*) Any sum paid by a public financial institution by way of contribution towards any fund (Exchange Risk Administration Fund) specified under clause (23E) of section 10.

Public Financial Institution shall have the same meaning as is assigned to it u/s 4A of the Companies Act, 1956.

GENERAL DEDUCTIONS (Section 37)

Section 37(1) says that any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the business or profession shall be allowed in computing the income chargeable under the head, "Profits and Gains of Business or Profession".

The deductions are to be allowed in respect of those expenses which shall satisfy the following conditions:

1. The expenditure should not be of the type of expenses already covered under sections 30 to 36 of this Act.

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2. Expenses should have been incurred in the relevant accounting year.
3. Expenses should be in respect of the business carried on by the assessee and the profits of which are to be computed and assessed, and should be incurred after the business is set up.
4. Expenses should not be in the nature of personal expenses of the assessee.
5. The expenses should have been incurred totally and exclusively for the purposes of the business of the assessee.
6. Expenses are not of capital nature.
7. The expenses are incidental to the business of the assessee and directly spring from the carrying on of it.
8. The reasonable expenditure towards payment of compensation to the employees whose services have been terminated would ordinarily come under the provisions of section 37(1). The said expenditure is allowed on the ground of commercial expediency. *(Sassoon David & Co. Ltd. v. C.I.T.).*
9. Deposit made under Own Your Telephone (OYT) scheme is admissible as expenditure *vide* circular letter No. F. No. 204/70/75-ITCA 11, Dated 10th May 1976.
10. Expenditure on deposit under Tatkal Telephone Deposit Scheme.

The entire amount of Rs. 30,000 paid under this scheme is allowed to be debited as Revenue expenditure. In case telephone is surrendered and some amount is refunded, such amount refunded shall be deemed as profit of the year in which refunded. [*CBDT Circular No. 671 Dt. 27.10.1993*]

Entertainment Expenditure [Section 37(2A)]

Entertainment expenditure has been defined in the explanation given in Section 37(2A) which includes:

(*i*) the amount of entertainment allowance granted by assessee to its employees or other persons.

(*ii*) the amount of any expenditure in the nature of entertainment expenditure [other than referred in (*i*)] incurred for the purposes of the business or profession of the assessee by any employee or other persons.

(*iii*) entertainment expenditure includes expenditure in provision of hospitality of every kind by the assessee to any person, whether by way of provision of food or beverages or in any other manner, and whether it is under any express or implied contract or customs or usage of trade but does not include expenditure on food or beverages provided by the assessee to his employees in office, factory or other place of work.

Any expenditure incurred by the employer in providing food and beverages was not to be treated as entertainment expenditure u/s 37(2) even if such facility was provided in places other than the place of work during working hours. With effect from assessment year 1996-97 a limit of Rs. 35 per day per employee has been imposed on such expenditure. If employer incurs an expenditure upto this limit it will not be treated as entertainment expenditure. Excess, if any, will be treated as

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entertainment expenditure for the purposes of section 37(2). (*Circular No. 708 dated 18.7.95)*

Any expenditure incurred by employer in providing food or beverages whether at the place of employment or outside but during working hours upto Rs. 35 per day per employee shall not be treated as income taxable under the head "Salaries" provided the amount is paid directly to the caterer, restaurant, eating place, canteen etc. Otherwise it will be treated as perquisite taxable in the hands of employees covered u/s 17(2) (*iii*) *i.e.* specified cases. (*Circular No. 708 Dated 18.7.95 as amended by Circular No. 727 dated 27.10.95)*

Expenditure on account of providing coffee, cigarettes etc. to customers has been held to be entertainment expenditure *[C.I.T. v. Veeriah Reddiar I.T.R. No. 54 of 1974]* and is allowed as per limits mentioned below.

New rates of deduction for entertainment expenditure [Section 37(2)]—With effect from previous year commencing on or after 1.4.92 entertainment expenditure shall be allowed as follows:

(*i*) If amount of expenditure does not exceed Rs. 10,000, actual expenditure or Rs. 10,000 p.a. whichever is less.

(*ii*) If amount of expenditure is more than Rs. 10,000—deduction to be allowed is Rs. 10,000 + 50% of expenditure exceeding Rs. 10,000.

This provision is being deleted with effect from assessment year 1998-99.

Advertisement through Souvenir of Political Parties

Section 37(2B) provides that notwithstanding anything contained in sub-section (1), no allowance shall be made in respect of expenditure incurred by an assessee on advertisement in any souvenir, brochure, tract, pamphlet or the like published by a political party.

Expenditure on Advertisement, Residential Accommodation Including Guest Houses and Travelling Expenses [Section 37(3)]

Any expenditure incurred by the assessee after 21.4.1964, on advertisement or on maintenance of any residential accommodation including any accommodation in the nature of the guest house or in connection will travelling by an employee or any other person (including hotel expenses or allowances paid in connection with such travelling) shall be allowed only to the extent and subject to such conditions, if any, as may be prescribed from time to time by the Board of Direct Taxes. The Board framed the rules regarding these items and these rules are applicable to expenditure incurred by the assessee after 10th August 1966.

Expenditure on Advertisements [Section 37(3) (Rule 6B)]

Expenditure incurred on advertisement shall be an allowable deduction but subject to the rules framed by the Board in this connection. According to rule 6B, allowance in respect of expenditure on advertisement shall not exceed the following:

(*a*) In case of articles intended for presentation the limits are as under :

(*i*) in case cost of one such item is upto Rs. 1,000 full cost is allowed; and

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(*ii*) in case cost is more than Rs. 1,000 per article—Rs. 1,000 + 50% of the balance cost shall be allowed and excess shall be disallowed.

(*b*) in respect of any advertisement outside India involving payment in foreign currency, only that amount shall be allowed and granted as permitted under the law relating to foreign exchange.

The A.O. is also empowered to disallow that part of the expenditure on advertisement which in his opinion is excessive or unreasonable having regard to the legitimate business needs of the assessee and the benefit derived by or accruing to him therefrom, the disallowance shall be only in case of the following payments:

(*i*) Where the payment is given to a person who has a substantial interest in the business of the assessee or to a relative of such person; or

(*ii*) Where the payment is given to a person who carries on the business of or profession, as a publicity or advertising agent and the assessee has a substantial interest in the business or profession of that person.

In case payment regarding advertisement expenses exceeding Rs. 10,000 is made otherwise than through a crossed cheque or by a crossed bank draft, such a payment shall not be allowed as deduction in computing the total income. [Section 40A(3) shall not apply in this case]

It is further provided that where in a previous year payment exceeding Rs. 10,000 is made otherwise than by crossed cheque or draft, the allowance for advertisement expenses made in that year shall be deemed to be wrongly made and provisions of section 155 shall apply.

Section 37(3) is being deleted with effect from assessment year 1998-99.

Expenses on installation of Neon signboards

All expenses incurred on the installation of neon signboards have been held to be an allowable expenditure falling within the category of expenses incurred on advertisement u/s 37(3) *[Mohan Meakin v. C.I.T. (1979) 148 I.T.R. 432].*

Guest House [Section 37(4)]

Under section 37(4)(ii) any expenditure incurred on the maintenance of guest houses after 28.2.1970 will not be allowed as deduction. Even the depreciation on the building and other assets used in a guest house is not allowed from the assessment year 1971-72.

Holiday Home

Sometimes, business undertakings run holiday homes for the benefit of their employees while on leave. Holiday homes are run at those places where the employees usually go during the holidays; normally these are set-up at important centres of tourist attraction and certain other important places. The expenditure incurred on the running and maintenance of the holiday homes will be an admissible deduction provided the unit fulfils certain conditions; these conditions are:

(*i*) The business unit is employing at least 100 whole-time workers throughout the relevant previous year.

(*ii*) The holiday homes are intended for the exclusive use of those employees while on leave.

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Any amount recovered or charged from the employees during their stay in the holiday homes will, however, be deducted from the expenditure incurred on the maintenance and running of such holiday homes.

Travelling Expenses of Employee and other Persons

Every business undertaking is required to incur some expenditure on the travelling of its employees and other persons (*e.g.*, Director of a company, partner of a partnership firm), while going outside in connection with the business work. For example, the salesmen move from town to town, the director or a partner may be required to attend the office of the Director of Industries, etc.

The travelling may be in India or outside India.

Travelling in India

When any employee or other person of the business goes outside the business headquarters, the amount of expenditure to be allowed as deduction will be limited to the aggregate of the following amounts:

(*a*) in respect of travel by rail, road, waterway or air the expenditure actually incurred;

(*b*) in respect of any other expenditure (including hotel expenses or allowance paid) in connection with such travel an amount calculated at the following rates for the period spent outside such headquarters:

in case expenditure is upto Rs. 1,500 per day—actual expenses are fully allowed; and

in case expenditure is more than Rs. 1,500 per day—Rs. 1,500 + 75% of balance shall be allowed. Excess is disallowed.

Travelling Outside India

Actual expenditure incurred on travelling outside India is allowed. The amount of foreign exchange allowed by the Government is an important factor in his case. In case the person going to a foreign country spends a few days for his private work etc., the proportionate expenditure of these days shall not be allowed as deduction.

Section 37(4) and 37(5) are being deleted with effect from assessment year 1998-99.

Legal expenses

Legal expenses incurred in the interest of the business are allowable expenses. The following types of legal expenses incurred in the interest of the business or profession are allowed under section 37:

(*i*) Legal expenses incurred in the normal course of the business;

(*ii*) To avoid a business liability, *i.e.*, compensation paid for breach of a contract in the interest of the business;

(*iii*) Legal expenses spent to defend the assessee's title of his business; and

(*iv*) To terminate a disadvantageous trading relationship.

The expenses which are of personal nature of the partner of the assessee are not treated as business expenses. Expenses incurred in criminal proceeding are also not considered to be incurred for a business purpose and so disallowed.

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Legal expenses incurred for curing any defect in the title (ownership) of asset are not allowed to be deducted. [V. Jagmohan Rao vs. C.I.T. (1970) 75 ITR 373 (SC)]

Legal expenses incurred while acquiring capital assets are not allowed, being the expenses of capital nature.

So, the most important test to be applied is whether a particular legal expenditure was incurred in the normal routine of the business and the expenditure was necessary to protect the business from disadvantage, loss etc.

Illustration 3. (*i*) Calculate the deduction admissible u/s 37(2) in respect of entertainment expenditure for assessment year 1997-98 from following information :—

Expenditure incurred on food provided to employees	Rs. 25,000
Entertainment Allowance paid to directors	Rs. 10,000
Other items of entertainment	Rs. 50,000

(*ii*) From the figures given below, find out the deduction admissible u/s 37(3) and the rules made there under in respect of expenditure incurred on advertisement in respect of Assessment year 1997-98 :

Expenditure on advertisement in a souvenir issued by a political party	Rs. 25,000
Expenditure on presentation articles :	
Value per article less than Rs. 1,000 per article	Rs. 25,000
Value per article—exceeding Rs. 1,000 (Number of articles-one)	Rs. 10,000
Expenditure incurred in cash	Rs. 12,000

Solution

(*i*) *Calculation of admissible entertainment expenditure for the assessment year 1997-98*

(*a*)	Expenditure incurred on food provided to employees (It is not to be considered for restriction u/s 37(2) explanation (*iii*) upto Rs. 35/- per day per employee)	Fully allowed
(*b*)	Entertainment Allowance paid to directors	10,000
	Other Entertainment Expenses	50,000
	Total	60,000

Restricted amount allowed u/s 37(2) will be Rs. 10,000 + 50% of balance of Rs. 50,000 [10,000 + 25,000] *i.e.* Rs. 35,000.

(*ii*) *Calculation of allowable advertisement expenditure*

(*a*) Expenditure on advertisement in a souvenir issued by a political party is not allowed u/s 37(2B).

(*b*) Expenditure on advertisement incurred in cash shall be fully disallowed as Rule 6B(3) has not been amended.

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(*c*) Expenditure on advertisement items is allowed upto Rs. 1,000 + 50% of balance cost per article. As such full expenditure of Rs. 25,000 will be allowed as cost per article does not exceed Rs. 1,000 per item. When cost of one article exceeds Rs. 1,000 per article *i.e.* Rs. 10,000, expenditure to be allowed will be Rs. 1,000 + 50% of Rs. 9,000 = Rs. 5,500.

Q. No. 3

A business house spent Rs. 52,000 on advertisement and publicity in the previous year 1996-97. This consisted of :

(*i*) Rs. 20,000 for hoardings, signboards and video cassettes.

(*ii*) Rs. 12,000 gifts to customers, made up of Rs. 2,000 articles of less than Rs. 1,000 each and Rs. 10,000, five articles of Rs. 2,000 each.

(*iii*) Rs. 5,000 cost of an advertisement in the souvenir of a political party.

(*iv*) Rs. 15,000 paid in cash for services of an advertising agency. The assessee does not have any valid reason for not paying by crossed cheque or draft.

Calculate the allowable amount of Advertising Expense.

[Karnataka B.Com. April 1995]

[**Hints :** (*i*) Fully allowed (*ii*) Allowed upto Rs. 2,000 + 7,500 = 9,500 (*iii*) Not allowed (*iv*) Not allowed under rule 6B. Total Allowed expenditure Rs. 29,500]

Expenses incurred on Raising Loans

According to a Supreme Court decision, the expenses incurred in connection with the raising of loans, issuing of debentures etc. (long-term or short-term) are an admissible deduction because these were incurred for the purpose of the business. The expenses included cost of stamps, registration fees, lawyer's fees etc.

On the other hand, expenses incurred on raising capital (*e.g.*, issuing of shares) are allowed in 10 instalments.

Allowable Deductions

The followings are some of the examples of expenses allowable as deduction u/s 37:

1. All expenses and payments made for purchasing of raw materials, manufacture and sale of goods.
2. All expenses in the nature of advertisement to push up sales and not covered u/s 37(3).
3. Sales-tax and expenses incurred in relation to sales tax appeal.
4. Day-to-day expenses to carry on business.
5. Some subscription to be paid compulsorily and to protect the business interests.
6. Reasonable expenses incurred at the time of mahurat, Dewali, etc. But no monetary ceiling has been fixed by Board.
7. Royalty paid in connection with the use of trade marks, patents, copyrights, etc.

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8. Commission paid to procure orders.
9. Compensation paid to an agent in connection with the termination or modifications in the terms and conditions of his agency.
10. Installation expenses of new telephone and payment made under 'Own Your Telephone' (O.Y.T.) scheme.
11. Expenses incurred to oppose the threatened nationalisation of the business. [Morgan V. Tata Lyle Ltd., 35 T.C. 367 (1944) 29 I.T.R. 195].
12. Legal expenses incurred to claim damages or compensation in case of non-fulfilment of a contract.
13. Pension, gratuity and any other voluntary payment given to the employees.
14. Gifts given to the employees but such gifts should not fall in the category of perquisites.
15. Bonus paid on the basis of an industrial award.
16. Any compensation paid to an employee on the termination of his service and also compensation paid to a managing agent on the termination of his agency.
17. Insurance premium paid to get insurance of employees against injury, accident while working and also any compensation paid to employees due to such injury or accident. Payment received from insurance company, if any, shall be treated as taxable income and credited to P & L A/c.
18. Expenses incurred on employees welfare activities.
19. Embezzlement by an employee during the normal course of the business.
20. Any payment given by the assessee to business rivals agreeing not to compete with the assessee.
21. Any compensation payable in the usual course of business including compensation paid as a result of negligence of the assessee or his employees.
22. Any expenditure incurred or compensation paid in lieu of getting the termination of disadvantageous trade contract or liability.
23. Penalty payable for delay in the execution of an order and even penalty payable for delay in the payment of sales tax shall be treated as usual business expenditure.
24. Any amount spent to make necessary alterations in the memo-randum of association and articles of association.
25. Any provision made for the payment of excise duty *[J.K. Synthetics v. O.S. Bajpai (1976) 105 ITR 864]*.
26. Any expenditure incurred on alterations and modifications made on premises got on lease provided the expenses are necessary for the proper utilisation of the premises.
27. Interest paid or payable on delayed payment of cash. This type of payment is not considered as penalty. *[Balrampur Sugar v. C.I.T. (1982) 135 ITR 227 (Cal.)]*.

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However, in an earlier judgement it was held that this type of penal interest is not allowable. *[C.I.T. v. Mahalaxmi Sugar Mills (1972) 85 ITR 320 (Del.)].*

28. Amount spent or payable to the Govt. in case of short-fall in the export target. *[Addl. C.I.T. v. Tarun Commercial Mills (1976) Tax (B) 48].*
29. Amount spent to preserve and protect business assets, interest and reputation. *[South Asia Industries v. C.I.T. (1981) 132 ITR 144 (Del.)].*
30. Amount paid to the landlord under a compromise to withdraw an eviction suit. *[South Asia Industries v. C.I.T. (1981) 132 ITR 144 (Del.)].*

Losses incidental to business. Following losses have been held to be business losses and can be debited to P & L A/c:

(*i*) Loss by theft and embezzlement by employee; *[Ram Gopal Ram Swaroop v. C.I.T. 47 ITR 611].*
(*ii*) Loss of cash due to robbery while being carried by cashier for disbursement;
(*iii*) Loss of cash by dacoity in case of a banking company;
(*iv*) Brokerage, commission and stamp duty incurred on rent deed for hiring office premises.
(*v*) Loss due to accidental fire in stock-in-trade.
(*vi*) Loss caused by white ants.
(*vii*) Loss caused due to theft of pledged goods.
(*viii*) Loss on sale of securities held by assessee as a trading asset.

Expenditure on civil defence measures to be treated as revenue expenditure [Circular No. 316 dated Sep. 30, 1981]

Any reasonable expenditure incurred by a business concern on civil defence measures both during emergency and when there is no emergency, would be allowed as revenue expenditure.

As already mentioned, many other expenses may arise at the time of actual running of the enterprise. The assessee should apply the test on the basis of conditions given earlier and if the expenditure satisfies those conditions then it will be legitimate charge on the profit of the business.

The real or actual net profit will be arrived at after deducting all the above-mentioned expenses incurred for the business.

EXPENSES EXPRESSLY DISALLOWED

Section 40 deals with such expenses which are totally disallowed in the computation of profit and gain of business or profession and so no deduction is allowed in respect of these expenses.

(*a*) In the Case of any Assessee u/s 40(*a*)

(*i*) *Interest paid outside India on money-borrowed.* This has already been explained on page 2/175.

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(*ii*) *Any other tax.* Any firm paid on account of any rate of tax levied on the profits or gain of any business or profession or assessed at a proportion of, or otherwise on the business of any such profits or gains is not allowed.

(*iii*) *Wealth-tax levied on Business Assets.* Wealth-tax which is levied on the assets of the business according to the Wealth-tax Act, 1957, will be allowed.

(*iv*) *Salary Payable outside India.* The payment of salary which is taxable under the head 'salaries' and is payable outside India the tax on this should be deducted at source or paid according to the law and if no tax is deducted, then the payment of salary will not be allowed as deduction while computing profit under business or profession.

(*b*) In the Case of any Firm [Section 40(*b*)]

The Finance Act 1992 has made the firm as a separate entity for income tax purposes and as such following new sub-section 40(*b*) has been inserted with effect from assessment year 1993-94:

In the case of firm assessable as firm (*i.e.* PFAF)

(*a*) any payment of salary, bonus, commission or remuneration by whatsoever name called, to any partner who is not a working partner shall be disallowed;

(*b*) any payment of remuneration to a working partner shall also be disallowed if such payment is not authorised by or is not in accordance with the terms of partnership deed;

(*c*) any payment of interest to a partner which is not authorised by or is not in accordance with the terms of partnership deed shall also be disallowed;

(*d*) any payment of remuneration to any working partner or of interest to any partner relating to the period (prior to the date of such partnership deed) for which such payment was not authorised or is not in accordance with, any earlier partnership deed, shall also be disallowed. However, the period of authorisation for such payment by any earlier partnership deed does not cover any period prior to the date of such earlier deed.

(*e*) any payment of interest to any partner which is authorised by and is in accordance with the terms of partnership deed and relates to the period falling after the date of such partnership is allowed if rate of interest does not exceed 18% p.a. If it exceeds 18% p.a. excess is disallowed;

(*f*) any payment of remuneration to all working partner which is in accordance with the terms of and is authorised by the partnership deed is allowed upto limits as laid down below:

1. In case of a professional firm covered u/s 44AA and so notified—the amount which can be debited is
   - (*i*) up to Book Profits of Rs. 1,00,000—Rs. 50,000 or 90% of Book Profit whichever is higher
   - (*ii*) next Rs. 1,00,000—upto 60% of Book Profit
   - (*iii*) on balance amount—upto 40% of Book Profit

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2. In case of any other firm

(*i*)	up to Book Profits of Rs. 75,000	—Rs. 50,000 or 90% of Book Profits whichever is higher
(*ii*)	next Rs. 75,000	upto 60% of Book Profit
(*iii*)	on balance amount	upto 40% of Book Profit

Excess over these limits is disallowed.

(*g*) In case a person is represented by another individual, in a firm such person is called "person so represented" and the individual who is so representing is called "partner in representative capacity".

(*i*) any interest paid to such individual (otherwise than as partner in representative capacity) shall not be taken into consideration for the purposes of this section;

(*ii*) any interest paid to such individual as partner in representative capacity and interest paid by the firm to the person so represented shall be taken into consideration for the purposes of this section.

(*h*) where an individual is a partner in a representative capacity, interest paid by the firm to such individual shall not be taken into account for the purposes of this clause, if such interest is received by him on behalf of or for the benefit of any other person.

(*i*) the term **Book Profit** means the net profit as shown in the profit and loss account for the relevant previous year computed in accordance with provisions of this chapter and after adding the aggregate amount of remuneration paid to partners if already debited to the Profit & Loss account or any other account prepared to calculate income.

(*j*) the term **working partner** means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner.

(*c*) General

The followings are the expense, allowances and losses which are also not allowed as deduction while computing income under the head 'profits and gains of business or profession':

(*i*) Drawings private or personal expenses of the proprietors partners etc.

(*ii*) Any expenditure in the nature of capital expenditure.

(*iii*) The amount paid as charity and presents. However, subscription is allowed.

(*iv*) Any provision or reserve except the special reserve of the approved financial corporations.

(*v*) Past losses (*i.e.*, loss of the past previous years) charged to profit and loss account.

(*vi*) Income-tax, Wealth-tax and any other tax which is imposed on income.

(*vii*) Any other expenditure which was incurred not necessarily, wholly and exclusively for the purposes of the business or profession of the assessee.

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(*viii*) Any provision for bad debts, taxation etc.

(*ix*) Depreciation in excess of the admissible amount under the provisions of the Income-tax Act, discussed in the next chapter.

Disallowing of certain Expenses under certain circumstances

Under section 40A, certain expenses otherwise allowable under the provisions of Income-tax Act, may not be deducted under the certain circumstances while computing income under the head 'business or profession'.

(*i*) Payments to relatives

Under section 40A (2), payments made or to be made to the persons or associate concerns of the assessee may be disallowed, if in the opinion of the Assessing Officer, such payments are considered to be excessive or unreasonable. If any portion of such payment is excessive or unreasonable, then that portion is to be disallowed.

The persons referred to above are the following namely:

(*i*)	Where the assessee is an individual.	any relative of the assessee;
(*ii*)	Where the assessee is a company, firm, association of persons or Hindu undivided family	any director of the company, partner of the firm, or member of the association or family, any relative of such director, partner or member;

(*iii*) Any individual who has a substantial interest in the business or profession of the assessee, or any relative of such individual;

(*iv*) a company, firm, association of persons or Hindu undivided family having a substantial interest in the business or profession of the assessee, or any director, partner or member of such company, firm, association or family, or any relative of such director partner or member;

(*v*) a company, firm, association of persons of Hindu undivided family of which a director, partner or member, as the case may be, has a substantial interest in the business or profession of the assessee or any director, partner or member of such company, firm, association or family or any relative of such director, partner or member;

(*vi*) any person who carries on a business or profession:

(*a*) where the assessee being an individual or any relative of such assessee, has a substantial interest in the business or profession of that person; or

(*b*) where the assessee being company, firm, association of persons or Hindu undivided family, or any director of such company, partner of such firm or member of the association or family, or any relative of such director, partner or member, has a substantial interest in the business or profession of that person.

As to what is excessive or unreasonable is an important factor which is to be determined having regard to the fair market value of the goods, services or facilities

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for which the payment is made or the legitimate needs of the business or profession or the benefit derived by or accruing to the tax-payer from the expenditure.

(*ii*) Payments exceeding Rs. 20,000 [Section 40A (3)]

To check the misutilisation of cash and to ensure that the payments are made to genuine persons, a clause under section 40A (3) was introduced to be applicable from the assessment year 1969-70. Under this clause, all payments exceeding Rs. 20,000 are to be made only through a crossed cheque or a crossed bank draft. So, if any payment exceeding Rs. 20,000 is made otherwise than through a crossed cheque or draft, then 20% of such amount is to be disallowed as deduction while computing income under this head of income.

The following are the exceptions:

1. Cash payments made under contracts entered into by the assessee before 1st April 1969.
2. Payment made in cash exceeding Rs. 20,000 under such circumstances as may be prescribed, having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors.

The Central Board of Direct Taxes has framed Rule 6-DD which provides for cases and circumstances in which payments exceeding Rs. 20,000 may be made otherwise than by a crossed cheque or a crossed bank draft. This rule provides that under the following cases no disallowance u/s 40A(3) shall be made where any payment of sum exceeding Rs. 20,000 is made otherwise than by a crossed cheque or a crossed bank draft:

1. Where the payment is made for the purchase of:
   (*i*) agricultural or forest product, or
   (*ii*) the produce of animal husbandry (including hides and skins) or dairy or poultry farming or
   (*iii*) fish or fish products, or
   (*iv*) the products of horticulture, to the cultivator, grower or producer of such articles, produce or products;
2. where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products;
3. where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, or profession or vocation, in any such village or town;
4. where any payment by way of gratuity, retrenchment compensation or similar terminal benefit, is made to an employee of the assessee or heirs of any such employee or in connection with the retrenchment, resignation, discharge or death of such employee, if the income chargeable under the head, "salary" of the employee in respect of the financial year in which such retirement, resignation, discharge or death took place or the immediately preceding financial year did not exceed Rs. 75,000;

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5. In case payment is made by an assessee as salary to his employee who is temporarily posted for a continuous period of more than 15 days at a place other than normal place of business or on a ship and such employee does not maintain a bank account at such place or at ship and tax as required u/s 192 has been deducted at source.
6. In case payment is made on such day or date on which banks are closed due to strike or holiday.
7. Where payment is made to an agent who is required to make further payment in cash. (*Notification no. 9917 dated 1.12.95*)

(*iii*) Provision for the Payment of Gratuity—u/s 40A(7)

With effect from 1.5.1976, on assessee shall be allowed as deduction in respect of any provisions made for the payment of gratuity to his employees on their retirement or on termination of their employment for any reason.

This provision shall not be applicable in the following cases:

(*i*) When the assessee makes a provision for any contribution towards an approved gratuity fund; or

(*ii*) When he makes a provision for the purposes of payment of any gratuity that has become payable during the previous year;

(*iii*) When the provision is made by the assessee for the previous year relevant to any assessment year commencing on or after 1.3.1973, but before 1.4.1976, to the extent the amount of such provision does not exceed the admissible amount subject to certain conditions.

Conditions

(*i*) The provision is made in accordance with actuarial valuation of the ascertainable liability of the assessee for payment of gratuity.

(*ii*) The assessee creates an approved gratuity fund and application for approval must have been submitted before 1.1.1976.

(*iii*) A sum equal to 50% of actual liability must be transferred to such fund before 1.4.1976 and balance of the actual liability before 1.4.1977.

Actual liability must be calculated in accordance with clause (*b*) of the rule 2 of part A of the Fourth Schedule.

Explanation 1

Admissible amount means an amount not exceeding $8^1/_3\%$ of employee's salary for each year of his service for which provision is being made.

Explanation 2

When the provision for gratuity is claimed and allowed, it cannot be claimed again when it is actually paid out of such fund.

(*iv*) Contribution to Funds, Trusts, Companies etc. [Section 40A(9)]

No deduction shall be allowed in respect of any sum paid by the assessee as an employer towards the setting up or formation of or as contribution to any fund, trust, company, association of persons, body of individuals or a society or other institution for any purpose except the contribution paid u/s 36(i)(v), (v-a) or (v).

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DEEMED PROFITS (Section 41)

(*i*) Deductions allowed earlier but recovered later on [Section 41(1)]

The Finance Act 1992 has substituted the sub-section 41(*i*) by the following with effect from assessment year 1993-94:

Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (here-in-after referred to as first-mentioned persons) and subsequently during any previous year—

(*a*) the first mentioned person has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by such person or value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly chargeable to tax as the income of that previous year whether the business or profession in respect of which the allowance or deduction has been made, is in existence in that year or not.

(*b*) in case such benefit or cash is obtained by successor in business in manner whatsoever in respect of which loss or expenditure was incurred by first-mentioned person the provisions mentioned in (*a*) above shall be applicable against such successor in business and he shall be liable to pay tax on such deemed profit.

The words successor in business means—

(*a*) in case of amalgamation—the amalgamated company;

(*b*) in case of succession—the successor;

(*c*) in case a firm is succeeded by another firm, such other firm.

For the purposes of this section the expression "loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof" shall include the remission or cessation of any liability by a unilateral act by the first mentioned person under clause (*a*) or the successor in business under clause (*b*) of that sub-section by way of writing off such liability in his accounts.

(*ii*) Profit on sale of assets used for scientific research [Section 41(3)]

Where capital asset was purchased for scientific research and is sold without having been used for any other purpose, excess amount of sale price added with the deduction allowed earlier over the capital cost of the asset is taxable as deemed income of the year in which sale was affected.

(*iii*) Bad debts allowed earlier but recovered [Section 41(4)]

Bad debts allowed earlier but recovered later on shall be deemed profits of the year in which they are recovered.

(*iv*) Amount withdrawn from special reserve [41(4A)]

With effect from assessment year 1998-99 following new point is being inserted:

In case a deduction has been allowed u/s 36(1)(*viii*) in respect of any amount transferred to special reserve and subsequently some amount is withdrawn from such

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special reserve, the amount so withdrawn shall be deemed as income under the head "Profits & Gains" of the year in which amount is withdrawn. This provision shall remain applicable even if the business is no longer in existance in the year in which amount is withdrawn.

(*v*) Setting off loss from deemed profit [Section 41(5)]

Any loss of a business incurred during the year in which it ceased to exist and which could not be set off against any other income of that previous year shall be set off against the above-mentioned deemed incomes. This does not apply to speculation loss.

VALUATION OF STOCK

The proper and correct valuation of stock is an important factor to arrive at the correct profits of any business undertaking. Correct or actual or real profits cannot be ascertained unless a proper method is adopted for the valuation of closing and opening stocks. The Income-tax Act is silent about this factor and so no method, whatsoever, is recommended by the Income-tax Act. Hence, it is valued according to the general accounting principles. An assessee may adopt any of the following methods for valuation of closing stocks—(*i*) at cost price, (*ii*) at market price, (*iii*) at cost or market price whichever is less. They are based upon the cost or market price of the stock, whichever is less. The businessmen are free to adopt any method, but once one method is adopted, the same is to be continued from year to year and the assessee cannot change the method of valuation to suit his own purposes. *[C.I.T. v. A.V. Apuchattair (1962) 45 I.T.R., 152. 155 Madras]*. It can only be changed with the prior approval of the Assessing Officer, *[Sir-Kikabhai Premchand v. C.I.T. 1953, 24 I.T.R. 596, 507 (S.C.)]*. Another point to be noted in this case is that the value of closing stock must be the value of opening stock in the succeeding year.

Under or over-valuation of stock. Generally the opening and closing stocks are not valued at cost price. They are either under-valued or over-valued. In such cases the profit of the year is affected by such under-valuation or over-valuation. To remove the effect of such valuation we adopt the following procedure:

(*i*) Bring the stock to real value in the following manner:

$$\text{Under-valuation} = \text{value of stock} \times \frac{100}{(100 - \text{rate of under-valuation})}$$

$$\text{Over-valuation} = \text{value of stock} \times \frac{100}{(100 + \text{rate of under-valuation})}$$

(*ii*) If opening stock is under-valued—calculate the difference between the actual value debited and value calculated above. It means the P & L A/c is under-debited by the amount of such difference. So profit is reduced by the amount of such profit.

(*iii*) If opening stock is over-valued—it will mean that P & L A/c has been over-debited by such difference. Hence increase the profit by such difference.

(*iv*) In case closing stock is under-valued—the P & L A/c is under-credited by the amount of such difference. So increase the amount of profit by such difference.

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(*v*) In case closing stock is over-valued—the P & L A/c is over-credited by the amount of profit by such difference. So reduced the amount of profit by such difference.

Value of goods drawn by proprietor for personal use

Such goods should be valued at cost price and not market price. No one can earn profit from himself *[Sri Cikabhai Premchand vs. Commissioner of Income-tax (1955) 24 I.T.R. 506 (S.C.)]*. As such in case the goods are drawn for personal use at the market price, the net profit must be reduced by the amount of profit earned from self by showing the withdrawal of goods at market price.

Profits of oil mining companies

Section 42 deals with certain allowances which are granted to those assessees, who carry on the business, in association with the Central Government, of prospecting for extracting or producing mineral oils.

Deduction of certain payments only if actually paid [Section 43 B]

Any payment of sales tax, employer's contribution to any provident fund, superannuation fund or gratuity fund, or any other fund for the welfare of employees will be allowed only in computing the income of that previous year in which such sum is actually paid by him. In case a deduction has already been claimed on accrual basis in any earlier previous year, it will not be allowed again in the year in which it is actually paid.

These payments are:

(*a*) any sum payable by the assessee by way of tax, duty, cess or fee by whatever name called, under any law for the time being in force, or

(*b*) any sum payable by the assessee as an employer by way of contribution of any provident fund, or superannuation fund or gratuity fund or any other fund for the welfare of employees.

(*c*) any sum referred to in clause (ii) of sub-section (1) of section 36, *i.e.*, bonus or commission payable to employees.

(*d*) any sum payable by assessee as interest on any loan or borrowing from any public financial institution or a State Financial Corporation or a State Industrial Investment Corporation in accordance with the terms and conditions governing such loans or borrowing.

(*e*) any sum payable by the assessee as interest on any term loan from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan. This provision will be applicable only on interest payable from 1.4.1996 onwards. In case any amount has been allowed as deduction in the year in which such liability was due upto 31.3.1996, it will not be allowed again in the year in which it is actually paid.

Deduction regarding these payments shall be allowed if such payments are actually made before filing of return u/s 139(1).

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Illustration 4. State the previous year during which the following expenses can be debited :

(*a*) Sales tax relating to previous year 1996-97 Rs. 20,000. Out of this amount Rs. 10,000 was paid on 5.4.97, Rs. 5,000 on 15.8.97 and Rs. 5,000 on 1-12-97. Date of filing of return is 31.8.97.

(*b*) Bonus of Rs. 1,40,000 relating to the previous year 95-96 was payable to employees in Dec. 1996 but was distributed in instalments on 1-12-96. Rs. 50,000 ; on 1-6-97 Rs. 50,000 and balance of Rs. 40,000 was paid on 1-11-97. The date of filing of return is 31-10-97.

(*c*) The provident fund deducted by employer out of employee's salary for March 1997 amounting to Rs. 29,400 was paid to Commissioner of Provident Fund by cheque on 15.4.97 but cheque was encashed on 2.5.97. Due date was 15.4.97.

Solution

(*a*) u/s 43 B any amount of sales tax paid during the year or before due date for filing of return is allowed to be debited in the same year to which it relates. As such amount Rs. 10,000 paid on 5.4.97 and Rs. 5,000 paid on 15.8.97 can be debited during the previous year 1996-97. But amount of Rs. 5,000 paid on 1-12-97 *i.e.* after due date of filing of return *i.e.* 31-8-97 can be debited during the previous year 1997-98 only.

(*b*) As per above the amount of Rs. 50,000 paid on 1-12-96 and Rs. 50,000 paid on 1-6-97 can be debited during 96-97 but amount of Rs. 40,000 paid on 1-11-97 *i.e.* after due date of filing of return *i.e.* 31.10.97 cannot be debited during 96-97. It can be debited during the previous year 1997-98 only.

(*c*) Payment of provident fund of Rs. 29,400 by cheque can not be debited during the previous year 1996-97 as cheque was not encashed within 15 days from due date.

Q. No. 4

From the information given below find out how much amount can be debited during the previous year 1996-97. These expenses relate to previous year 1996-97.

S. No.	*Expenses*	*Amount and Date of Payment*	*Due date*
1.	Interest to Financial Corporation	Rs. 100,000 on 1-6-97 Rs. 100,000 on 31-3-98	31-10-97
2.	Employer's contribution to Provident Fund	Rs. 20,600 on 13-4-97 by cheque which was encashed on 26-4-97	15-4-97
3.	Advance Income Tax	Rs. 62,000 on 29-10-97	31-10-97
4.	Excise duty	Rs. 1,40,000 paid on 1-1-98	30-11-97

[Hints (*a*) Rs. 100,000 paid on 1-6-97 ; (*b*) Rs. 20,600 (*c*) Not allowed (*d*) NIL.]

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Special provisions in case of income of public financial institutions etc. [Section 43D]

(*i*) In case of—
  (*a*) public financial institutions; or
  (*b*) a scheduled bank; or
  (*c*) a state financial corporation; or
  (*d*) a state industrial investment corporation;

(*ii*) there is some income as interest in relation to bad debts or doubtful debts;

(*iii*) which are prescribed by the appropriate authority having regard to guidelines issued by RBI;

(*iv*) such interest shall be chargeable to tax in the previous year in which it is actually received or is credited to profit & loss account, whichever is earlier.

Computation of profits of insurance business (Section 44)

Notwithstanding anything to the contrary contained in the provision of this Act relating to the computation of the income chargeable under the head, "Income from House Property", "Capital Gains", "Income from other sources" or in section 199 or sections 28 to 43A, the profits and gains of any business of Insurance, including any such business carried on by a Mutual Insurance Company or by a co-operative society, shall be computed in accordance with the rules contained in the First Schedule.

Computation of income of trade, professional or similar associations (Section 44A)

Where in case of trade or profession or similar type of other associations, the amount received from its members by way of subscriptions, or otherwise is less than the expenditure incurred by such association, the deficiency shall be allowed to be set off from the income of such association under head "Profit and Gains of Business or Profession" and if the income under this head is not sufficient to meet the deficiency, it can be set off from any other head of income.

The expenditure must have been incurred by such association during that previous year solely for the purposes of advancement, or protection of common interest of its members.

Before setting off such deficiency, effect shall be given to any other section of this Act regarding set off and carry forward of losses. The amount of deficiency to be allowed as deduction under this section shall, in no case exceed 7.5% of total income of such associations before allowing this deduction.

Maintenance of accounts [Section 44AA]

I. **For specified professions.** In case a person is carrying on any of the following professions as specified u/s 44AA, he is required to maintain his accounts in prescribed manner as given below:

A. Specified profession

Accountancy, Architecture, Engineering, Legal, Interior decoration, Medical, Technical consultancy or any other profession to be notified by the Central Government.

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The professions of authorised representative (who represents any other person on payment of any fee or commission before any tribunal etc.) and film artists have been so notified.

B. Prescribed manner for maintenance of accounts

1. In case gross receipts of the profession during the previous year or in any of the three preceding previous years or in case of a newly started profession **is not likely to exceed Rs. 60,000 (Rs. 80,000 in case of medical profession)**—the accounts are to be maintained in such manner as may enable the Assessing Officer to compute the professional income.

2. In case professional receipts exceed, or have exceeded in any of the three preceding previous years or are likely to exceed (in case of newly started profession) **Rs. 60,000 (Rs. 80,000 in case of medical profession)**—the accounts are to be maintained in the manner prescribed by the Central Board of Direct Taxes (C.B.D.T.). The procedure has been prescribed in Rule 6F of the Income-tax Rules 1962.

II. For unspecified profession. In case a person is not carrying on any of the professions specified above the prescribed manner for maintenance of accounts are—

1. if income from such unspecified profession, or total sales/turnover or gross receipts during relevant previous year do not exceed or in any of the three preceding previous years have not exceeded or in case of a newly started profession are not likely to exceed Rs. 40,000 or Rs. 5,00,000 respecti-vely, accounts are to be maintained in any manner assessee desires.
2. if income or turnover in above case exceeds Rs. 40,000 or Rs. 5,00,000 respectively the accounts are to be maintained in such manner which may enable the Assessing Officer to compute the professional income.

Compulsory audit for the non-corporate assessees (44 AB)

Every assessee who fulfils either of the following two conditions, shall have to get his accounts audited. The audit must be got done before the specified date and copy of the report duly signed and verified in prescribed manner must be furnished before such specified date.

Conditions

1. If a person is carrying on business—his total sales, turnover or gross receipts in business exceed Rs. 40 lakhs in a previous year.

OR

2. If a person is carrying on profession—his gross receipts in profession exceed 10 Lakh rupees in a previous year.

In case the accounts of a person are being audited under the provisions of any other laws or under any other provision of this Act, the report so obtained will be sufficient for this purpose.

Specified Date is the date by which the person is required to file return of his income as prescribed u/s 139.

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The provisions of section 44AB shall not be applicable on such persons who derive incomes mentioned under section 44 B, 44 BB, 44 BBA or 44 BBB on and from 1.4.85 or as the case be, the date on which relevant section came into force.

This amendment has been made by the Finance Act 1992 with retro-spective effect from 1.4.85.

Profit From the Business of Civil Construction or Supply of Labour [Section 44 AD]

The Finance Act 1994 has added this section with effect from assessment year 1994-95 and it provides for fixation of minimum profits for the business of civil construction or supply of labour. The limit is :

(*i*) The Profit declared in the annual return filed ; or

(*ii*) a sum equal to 8% of the gross receipts paid or payable to the assessee during the previous year on account of such business :

whichever is higher.

Rules :

(*i*) The above section will not be applicable in case of those assessees whose gross receipts **exceed Rs. 40 lakhs.**

(*ii*) In case "*8% of gross receipts*" is taken as profit, it will be presumed that all the expenses allowable u/s 30 to 38 and 40(b) have been debited.

(*iii*) For written down value of depreciable assets it will be presumed that full depreciation allowable under Income-tax Act has been calculated and given effect for next year's depreciation.

(*iv*) For calculating the monetary limits under section 44 AA and 44 AB, the gross receipts of above business shall be excluded. In case of the business covered u/s 44 AD, the provisions of section 44 AA and 44 AB shall not apply.

(*v*) In case Assessing Officer is satisfied on the basis of evidence produced by the assessee that the profit of such business is actually less, he shall proceed to make assessment u/s 143 (3).

Profit from the Business of carriage of Goods [Section 44 AE]

With effect from assessment year 1994-95, the Finance Act 1994 has inserted the following new section.

1. This section is applicable only on those persons who are engaged in the business of plying, hiring or leasing goods carriages and who owns **not more than 10** such goods carriages.
2. This section has fixed monthly income chargeable to tax as business profit in respect of each type of vehicle which is as under :
   (*a*) In case of heavy duty (goods) vehicle an amount equal to Rs. 2,500 (for other vehicles Rs. 2,000) per month or part of the month during which the vehicle is owned by the assessee during the previous year.

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(*b*) In case actual income declared by assessee is more than the above limits, than the actual income shall be subject to tax.

(*c*) In case Assessing Officer is satisfied that the income of the person is less than the prescribed limits, he shall make the regular assessment u/s 143 (3).

3. In case monetary limits of profit are adopted, it will be presumed that all the expenses u/s 30 to 38 and 40(b) have been deducted.
4. It will also be presumed that full depreciation has been calculated and deducted for calculating written down value of the assets.
5. The provisions of section 44 AA and 44 AB shall not be applicable on such business and for calculating monetary limits the gross receipts or the income shall not be considered.

Profits & Gains if retail business—special provision [Section 44AF]

With effect from assessment year 1998-99 :

(*a*) In case of a person who is engaged in retail trade in any goods or merchandise.

(*b*) Where total turnover during the previous year does not exceed Rs. 40 lakhs.

(*c*) Shall pay tax on deemed profits to be calculated @ 5% of total turnover in the previous year or on actual profits as declared by the assessee in his return of income.

(*d*) It shall be deemed that assessee has claimed all the expenses as given u/s 30 to 38 and 40(b).

(*e*) It shall be deemed that W.D.V. of the asset has been calculated after allowing and adjusting full depreciation as is admissible.

(*f*) Provisions of section 44AA and 44AB shall not be applicable and the income from such business shall be excluded for computing total turnover.

(*g*) The assessee shall be entitled to prove that his income is below the above mentioned amount and in such case regular assessment shall be made.

Computation of profits and gains of non-resident—44B

In case of an assessee being a non-resident carrying on the business of operation of ship, a sum equal to 7.5% of the aggregate of the amounts specified below shall be deemed to be profits and gains of such business.

Amounts

(*i*) The amount received by assessee or by an other person on his behalf or an account of carriage of passengers, livestock, mail or goods shipped at any port in India; and

(*ii*) The amount received or deemed to be received in India by or on behalf of the assessee on account of carriage of passengers, livestock, mail or goods shipped at any port outside India.

The amounts referred above shall include the amount paid or payable or received or deemed to be received, as the case may be, by way of demurrage or handling charges or any other amount of similar nature.

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Computation of Profits and Gains of business of oil exploration (44BB)

In case of an asseessee being non-resident engaged in the business of providing services or facilities in connection with or supplying plant & machinery on hire used or to be used in prospecting for or extraction or production of mineral oils a sum equal to 10% of the aggregate of the following amounts shall be deemed as profit of such non-resident assessee for income-tax purposes. The amounts are:

(*a*) amount payable or paid (whether in India or out of India) to the assessee for providing facilities in connection with or supply of plant & machinery on hire basis for using in prospecting or exploration or production of mineral oils in India; or

(*b*) any such amount for exploration or production of mineral oils outside India.

Computation of profits and gains of the business of operation of aircrafts by non-resident [Section 44 BBA]

In case a non-resident assessee receives following amounts:

(*a*) amount paid or payable (whether in India or out of India) to the assessee on account of the carriage of passengers, livestock, mail or goods from any place in India; and

(*b*) any such amount [mentioned in (*a*) above] from any place outside India.

—a sum equal to 5% of the aggregate of above-mentioned amounts shall be deemed as profit of the year.

Computation of profits of foreign enterprises [Section 44 BBB]

In case a foreign enterprise which is a foreign company, is engaged in the business of civil construction or business of erection of plant or machinery or testing or commissioning thereof in connection with a turnkey power project approved by the Central Government and financed under any international aid programme, a sum equal to 10% of the amount paid or payable (whether in India or outside India) on this amount shall be deemed to be the profit of such business chargeable to tax under this head.

Ceiling limits in respect of head office expenses [Section 44C]

According to this amendment, the foreign companies operating in India through branches, shall be entitled to a deduction in respect of head office expenditure and it will be limited to:

(*a*) an amount equal to 5% of the adjusted total income of the tax-payer for the relevant year; or

(*b*) the actual amount of head office expenditure attributable to the business in India, whichever is the least.

Computation of royalty income of foreign companies [Section 44D]

The deduction to be allowed in computing the income by way of royalty or fee for rendering technical services received from an Indian concern by a foreign company shall be limited to 20% of gross amount of such income received as per agreement entered before 1.4.76. No deduction is to be allowed if such income is received as per agreement entered after 31.3.76.

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Commission earned by the agents of Life Insurance Corporation, Unit Trust of India, Post Office or Mutual Funds

Out of Commission earned by the agents of above mentioned institutions an ad-hoc deduction is allowed in following manner :—

A. If amount of commission exceeds Rs. 60,000 in a previous year

No ad-hoc deduction is allowed. The agent can claim expenses as per provisions of section 30 to 43B of the Act.

B. If amount of commission does not exceed Rs. 60,000 in a previous year

(*i*) For agents of U.T.I., Post Office and Mutual Funds.....an ad-hoc deduction of 50% of such commission is allowed.

(*ii*) For agents of L.I.C.....

(*a*) If separate figures of first year and renewal commission are available.....an ad-hoc deduction of 50% of first year's commission + 15% of renewal commission subject to a maximum of Rs. 20,000 is allowed.

(*b*) If separate figures are not available—$33^1/_3$% of commission subject to maximum of Rs. 20,000 shall be allowed as ad-hoc deduction.

(*c*) Out of bonus commission no ad-hoc deduction is to be allowed.

Partly Agricultural and partly business income

Income from tea grown and manufactured. Income derived from the sale of tea grown and manufactured by the assessee in India is considered to be business income. Under rule 8 of the Income-tax Rules, 1962, 40% of the profit derived from tea industries shall be business income and remaining 60% is treated as agricultural income. So the profits of such business are partly taxable and partly non-taxable, 40% of profits are taxable as business profit and 60% profits are treated as agricultural income.

Sugar Mill Companies—One adjustment is to be noted carefully in case of sugar mill companies owning their own agricultural farms.

In such cases, the profit and loss account of the sugar mill is to be debited with the market value of the sugarcane crushed and grown in their own farms and cultivation expenses of the sugarcane grown in own farm are not to be debited to the profit and loss account. By this adjustment, the profit derived from the running of the agricultural farm can be allocated and so this profit will not be taxable as agricultural income.

Adjustment in the profit and loss A/c prepared by the assessee

All the assessees are required to prepare their profit and loss account according to the provisions given in the Income-tax Act and only those expenses are to be allowed as deduction which are actually allowable expenses. But sometimes, assessees prepare their profit and loss account without adhering to the provisions of Income-tax Act. In such cases the persons are supposed to correct the profit and loss account prepared by the assessees in the light of the provisions of law.

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The following are the important mistakes committed by the assessees while preparing their profit and loss account:

(*i*) Certain expenses are charged or debited to the profit and loss account but these expenses are not admissible either fully or partly.

(*ii*) Certain admissible expenses are omitted from charging.

(*iii*) Certain incomes are not credited to the profit and loss account.

(*iv*) Certain other income not falling under this head of income are unnecessary credited to the profit and loss account.

How to adjust such Mistakes or Irregularities?

1. The expenses which are not allowed but charged to the profit and loss account, the amount of such expenses are to be added back in the profit given in the profit and loss account. On the other hand, if any expense is omitted or lesser amount is charged, then the actual amount is allowed to be deducted from the profit given. If any expenses is charged in excess, the excess part is to be added in the profit given.
2. If any income or receipt related to the business or profession of the assessee is omitted, the amount so such receipt is to be added in the profit given.

On the other hand, if any income not related to the business is added on the credit side of the profit and loss account, then the amount of such item is to be deducted from the profit given.

CHART SHOWING COMPUTATION FOR PROFITS AND GAINS OF BUSINESS OR PROFESSION

Computation of Business Profits

For computation of Business profits, the Profit and Loss Account serves as the basis. The profit and loss account shows certain expenses and losses which are either fully or partly disallowed under the provisions of Income-tax Act. On the credited side there are certain incomes which are either tax-free or are not taxable under this head. The following table can help a person to compute the business income of an assessee:

Balance as per P and L A/c	*Profit (+) Loss (–)*	*Rs. Amount*
I. Add expenses claimed but not allowed under the Act		
(*i*) All provisions and reserves (Reserve for bad debts/Depreciation/Income Tax etc.) except creation of reserve by financial corporations u/s 36	—	
(*ii*) All taxes (*i.e.*, Income Tax, Advance Income Tax, Wealth Tax etc.) except Sales Tax, Excise duty and Local taxes of premises used for business	—	
(*iii*) Rent paid to self	—	
(*iv*) All capital expenses except on scientific research	—	
(*v*) All capital losses	—	
(*vi*) All charities and donations	—	
(*vii*) All expenses relating to other heads of income (*e.g.*, Taxes on house property etc.)	—	

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Balance as per P and L A/c	*Profit (+) Loss (–)*	*Rs. Amount*
(viii) Cultivation expenses	—	
(ix) Any interest on capital unless the amount is borrowed	—	
(x) All personal expenses (Drawing etc.)	—	
(xi) Any depreciation if wrongly debited	—	
(xii) Gifts and presents	—	
(xiii) Any type of fine or penalty	—	
(xiv) Any payment to a partner (In case of firms only by way of salary, interest, bonus, commission or remuneration excess over prescribed limits)		
(xv) Any salary or interest payable outside India unless tax is deducted at source or is paid according to the law	—	
(xvi) Past losses (*i.e.*, loss of the past years)	—	
(xvii) Any other expenditure which is not incurred according to the provisions of law,	—	
(xviii) Salary paid to self or any other member of family for casual help	—	
(xix) Personal life insurance premiums	—	
(xx) Any amount invested in savings such as NSS, NSC, PPF etc.	—	
(xxi) Rent for residential portion	—	
(xxii) Speculation loss	—	
(xxiii) Bad Debt still recoverable	—	
(xxiv) Legal expenses on criminal case; or a personal case of employee	—	
(xxv) Expenses on maintenance of Guest houses	—	
(xxvi) Expenses on maintenance of holiday home if number of workers is less than 100	—	
(xxvii) Entertainment expenses exceeding prescribed limit	—	
(xxviii) Legal expenses on acquiring an asset	—	
(xxix) Advertisement expenses-distribution of items cost exceeding prescribed limits	—	
(xxx) Travelling & Hotel expenses of employees exceeding prescribed limits	—	
(xxxi) Investment allowance, Investment deposit account, Development allowance	—	
(xxxii) Cash shortage	—	
(xxxiii) Loss by theft from residence	—	
(xxxiv) Expenses on illegal business	—	
(xxxv) Employer's contribution to unrecognised provident fund	—	
(xxxvi) Difference in trial balance	—	
(xxxvii) Difference due to under crediting of stock	—	
(xxxviii) Cost of Patent rights being capital expenditure		
(xxxix) Cost of Technical know-how being capital expenditure		
(xl) Preliminary expenses being capital expenses. Total of these items is added in the profit or is adjusted out of the loss	—	
	—	
		A

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II. Deduct [out of the amount arrived at (A) above] any expenditure which is allowable under the Act, but has not been debited to P and L A/c:

(*i*)	Actual bad debts (not charged in P and L A/c)	—
(*ii*)	Depreciation (—do—)	—
(*iii*)	Any other expenditure incurred according to provision of law	—
(*iv*)	Difference due to under debiting of stock	(–)
	Total of these is deducted from (A) above and we get	(B)

III. Deduct out of the amount arrived at (B) above any income which is either exempt or not taxable under this head:

(*a*) *Incomes exempted from tax*

(*i*) Post office saving bank interest
(*ii*) Agricultural receipts
(*iii*) Gifts from relatives
(*iv*) Income-tax refund
(*v*) Bad debt recovered—disallowed earlier
(*vi*) Life Insurance Maturity Amount
(*vii*) Any capital receipt
(*viii*) Withdrawal from PPF

(*b*) *Incomes taxable under other heads*

(*i*) Part-time salary
(*ii*) Interest on Securities
(*iii*) Rent from House property Let
(*iv*) Capital gains
(*v*) Dividend, Bank Interest, winnings from Lotteries, race course etc.

Total of these is deducted from (B) above and we get taxable profit from the business.

Add: Income from any other business (legal or illegal) to get income taxable under the head Profits & Gains of Business or Profession.

Computation of Professional Income

The above-mentioned method is not suitable to compute professional income because professional persons usually do not prepare profit and loss account. They prepare Income and Expenditure Account of Receipts and Payment Account. To compute the professional income, it is easier to take professional receipts of the previous year and deduct out of these the professional expenses incurred during that year.

The following illustration can help a person to compute the personal income of an assessee.

In case of Doctor or Medical Practitioner

Professional Receipts	*Amount*
(*i*) Consulation fees	—
(*ii*) Operation fees	—
(*iii*) Visiting fees	—
(*iv*) Sale of medicines	—

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(v) Gift from patients (because these are received as token of gratitude for professional services rendered)	—	
(vi) Value of any perquisite received by such person	—	
(vii) Examiner's fees	—	
(viii) Nursing home receipts	—	
(ix) Any other professional receipt	—	
Total Receipts		
***Less* : Professional Expenses**		
(i) Dispensary Expenses (*i.e.*, rent, light, water charges, salary to staff, telephone expenses etc.)	—	
(ii) Opening stock plus Cost of medicines less closing stock	—	
(iii) Depreciation on Surgical Equipment and X-ray Machines, etc., at prescribed rates	—	
(iv) Cost of books for professional purposes	—	
(v) Motor car expenses: depreciation relating to professional work	—	
(vi) Expenditure incurred to increase professional knowledge	—	
(vii) Nursing home expenses	—	
(viii) Any other expenditure incurred during the year	—	—
Professional Income	—	—

In case of Chartered Accountant

Professional Receipts	*Rs.*	*Amount*
(i) Audit fees	—	
(ii) Income from accountancy work	—	
(iii) Institute fees	—	
(iv) Examiner's fees	—	
(v) Gifts from clients, if any	—	
(vi) Consultancy Services	—	
(vii) Any other receipt	—	
Total Professional Receipts		—
***Less* : Professional Expenditure**		
(i) Office expenses	—	
(ii) Institute expenses	—	
(iii) Cost of books	—	
(iv) Motor car expenses relating to professional work	—	
(v) Membership fees	—	
(vi) Depreciation on office equipment, car or scooter etc.		
(vii) Any other expenditure incurred to increase professional knowledge	—	
(viii) Stipend to trainees	—	
(ix) Subscriptions	—	
(x) Dep. on office furniture	—	
Total Professional expenses		(—)
Professional Income		—

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III. Income of a Lawyer or an Advocate

Professional Receipts

(*i*)	Practicing fees	—	
(*ii*)	Legal fees	—	
(*iii*)	Special commission	—	
(*iv*)	Presents from clients	—	
(*v*)	Examiner's fees	—	
(*vi*)	Any other receipt	—	
	Total Professional Receipts	—	—

Less : **Professional Expenses**

(*i*)	Office expenses	—	
(*ii*)	Salary of staff, if any	—	
(*iii*)	Cost of books for professional purposes		
(*iv*)	Depreciation of office equipment	—	
(*v*)	Expenditure incurred to increase professional knowledge	—	
(*vi*)	Subscription	—	
(*vii*)	Purchase of stamp paper and court fee	—	
(*viii*)	Travelling expenses		
	Total Professional Expenses	(–)	×××
	Professional Gain		×××

Illustration 5. State whether the following items are deductible or not and why.

1. Sales-tax and Wealth-tax.
2. Donation to a political party.
3. Cost of installing a new telephone.
4. Fees paid to the lawyer for drafting partnership deed.
5. Loss due to embezzlement by an employee.
6. Penalty paid to custom authorities for violating custom rules.
7. Commission paid while purchasing raw materials.
8. Some amount paid to a labour leader to call off the strike.
9. Bad debts.
10. In the course of money-lending business, the assessee acquired certain properties in lieu of debts and held them as stock-in-trade. The properties so acquired were destroyed by enemy action and the assessee claims the loss as deduction.
11. Brokerage paid for raising a loan.
12. Rs. 1,000 were snatched from the cashier while he was going to the bank to deposit the amount.
13. Legal expenses paid to protect the building of the business.
14. Rs. 5,000 paid as a commission to purchase machinery and Rs3500 were also spent as travelling expenses on the person who went to purchase the machinery.
15. Subsidy received under export promotion scheme from Government.

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Solution

1. Wealth-tax is expressly disallowed. Wealth-tax is levied on the value of assets and so this tax has nothing to do with the carrying on the business. It is tax on wealth and is not payable while earning profit.

The payment of tax on sales in the normal running of the business and is made for the purpose of the business. Sales-tax in an admissible deduction.

2. Few years back, this type of donation was allowed but now the donation to a political party is not an allowable deduction. This amount is disallowed on the ground that it has nothing to do with the purposes of the business.

3. To a layman and to the students of accountancy, this expenditure seems to be capital expenditure. Under executive instructions, the cost of installing a new telephone is an admissible deduction.

4. Expenditure incurred on drafting a partnership deed is a capital expenditure and so it is not an admissible deduction.

5. The employees of the business have access over cash in the business and in routine or normal running of the business, embezzlement of cash by employee is possible. As this loss occurs in the ordinary course of the business, so it is an admissible item.

6. Penalty was imposed upon the assessee for his illegal work. So penalty paid on illegal work cannot be allowed as deduction.

7. This type of commission is paid in the ordinary course of the business and for the purpose of the business, so it is an admissible deduction.

8. If the receipt of voucher of this type of expenditure is available, then this item can be an allowable item because the payment was made in the interest of the business. It may not be allowable item due to non-availability of proof of this type of payment.

9. In the ordinary course of the business few debtors or some percentage of debtors normally do not pay. So the debts which are not recoverable and actually written off in the books of the assessee, are allowed as deduction.

10. This loss is allowable as it is the loss of stock-in-trade. The properties were kept as stock-in-trade.

11. Brokerage paid for raising a loan for the purpose of the business is an allowable deduction. However, brokerage paid for raising capital is not allowed.

12. This type of loss is considered as revenue loss, so it is an allowable deduction.

13. Expenditure incurred to protect the interest of the business is an allowable expenditure. So the legal expenses are allowed as deduction.

14. Commission paid to purchase a capital asset is a capital expenditure. Expenses incurred on travelling are also treated as capital. So Rs. 3,500 cannot be allowed as deduction, being a capital expenditure. These are added to the cost of asset.

15. Any subsidy received by an assessee as an export subsidy under an export-promotion scheme promulgated by Government was held to be taxable income from business u/s 28. *[C.I.T. v. Swadeshi Cotton Mills Co. Ltd. (All)]*.

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Illustration 6. Discuss how the following items are to be dealt with in the income-tax assessment of a company:

(*a*) Capital expenditure on scientific research Rs. 4,00,000.

(*b*) Expenses by way of brokerage, stamps fees, lawyer's fees etc. amounting to Rs. 90,000, for raising a long-term loan of Rs. 10,00,000.

(*c*) Preliminary expenses before the commencement of production Rs. 1,60,000.

(*d*) Payment in U.K. of salaries and interest amounting to Rs. 80,000 and Rs. 30,000 respectively without deduction of tax at source.

(*e*) Expenses incurred in respect of a branch of the business which was discontinued by the assessee during the accounting year.

(*f*) Expenses for shifting an industrial undertaking from the urban to rural area.

(*g*) Income-tax paid on behalf of a non-resident in respect of whose income the assessee was assessed as agent.

(*h*) Expenditure incurred outside India to promote the sales of the company although no sale was made during the accounting year.

(*i*) Provision of Rs. 2,80,000 for doubtful debts.

(*j*) Payment of Rs. 15,000 to a lawyer—for preparing Income-tax return Rs. 10,000 and Rs. 5,000 for filing a suit regarding income tax assessment of an earlier year.

Solution

(*a*) Capital expenditure on scientific research is an allowable or admissible deduction u/s 35 while calculating company's income under the head 'business'. The entire capital expenditure is allowed as deduction in the previous year in which such an expenditure was incurred provided the profit is available in the year. If profit is not available, the amount of expenditure in this account is allowed to be carried forward till it is fully written off.

(*b*) Expenses incurred on raising loan (*e.g.*, stamp duty/fees, lawyer's fees, brokerage etc.) are allowed to be deducted u/s 37 (1). The loan arranged may be short-term or long-term.

(*c*) Preliminary expenses of Rs. 1,60,000 (provided such preliminary expenses do not exceed $2^1/_2\%$ of the cost of the project) are amortized in 10 years *i.e.*, 1/10th of preliminary expenses are charged every year beginning with the assessment year in which the actual production begins.

(*d*) Any payment like salaries, interest on money borrowed etc. paid to non-resident person shall be allowed as deduction only if tax is deducted at source out of such payment made. Since no tax was deducted in the said case, so these payments are not admissible u/s 40 (*a*) (*i*) and (*ii*).

(*e*) With the discontinuance of assessee's business, the previous year automatically comes to an end and assessee cannot claim any deduction

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regarding expenses incurred in respect of any business which has been discontinued by the assessee. Even if a person is carrying on some business in another branch, it does not entitle him to set off loss of a discontinued branch from income of another branch.

(*f*) Expenses incurred to shift an industrial unit from an urban to rural area are of capital nature and as such would not qualify for deduction u/s 37(1). It is also not to be added in actual cost of unit for depreciation. *[Sitapur Sugar Works Ltd. v. C.I.T. (49) I.T.R. (S.C.) 160].*

(*g*) Income-tax paid on behalf of a non-resident cannot be allowed as deduction. The law does not entitle any tax-payer to negotiate or transfer his tax liability with any other person.

(*h*) Actual expenditure is allowed.

(*i*) The provision made for bad and doubtful debts of Rs. 2,80,000 cannot be allowed as deduction and if already claimed, the same would be added back to company's business income.

(*j*) Fully allowed to be debited as restriction u/s 40 A(12) has been deleted.

Illustration 7. From the following Profit and Loss Account of M/s ABC firm, calculate the income under the head 'Profits and Gains of Business or Profession'.

	Rs.		Rs.
General Expenses	5,000	Gross Profit	40,000
Fire Insurance Premium	1,000	Bad debts, recovered but disallowed earlier	4,000
Bad debts	1,000	Interest from Govt. Securities	4,000
Salaries	5,000		
Advertisement	2,250		
Proprietor's salary	2,500		
Interest on capital	2,000		
Income-tax	1,000		
Depreciation	2,000		
Sales-tax	5,000		
Advance income-tax paid	1,000		
Donations	500		
Motor car expenses	750		
Net Profit	19,000		
	48,000		48,000

General expenses include Rs. 440 paid as compensation to an old employee whose services were terminated in the interest of the business and Rs. 200 by way of help to a poor student. Depreciation calculated according to the rates comes to Rs. 2,900.

50% of Motor-car expenses are for proprietor's personal use.

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Solution

Computation of business profit of M/s ABC firm.

		Rs.
Profit as given in the Profit and Loss Account		19,000
Add: Inadmissible Expenses		
Proprietor's salary	Rs. 2,500	
Interest on capital	2,000	
Income-tax	1,000	
Depreciation	2,000	
Advance Income-tax paid	1,000	
Donations	500	
50% of car expenses being incurred for proprietor's personal use	375	
Help to a poor student	200	
		9,575
		28,575
Less: Allowable expenses		
Depreciation		2,900
		25,675
Less: Incomes not taxable under this head		
(*i*) Bad debt recovered but disallowed earlier (being exempted)	Rs. 4,000	
(*ii*) Interest on Govt. Securities	Rs. 4,000	
		8,000
Business Profit		17,675

Notes : (*i*) Deduction of donations u/s 80G is to be allowed from the Gross Total Income.

(*ii*) Interest on Government Securities is taxable under the head 'Income from other sources'.

(*iii*) Bad debts recovered cannot be taxed now, as this amount was taxed earlier when the Assessing Officer disallowed this item.

Illustration 8. From the following Profit and Loss Account of a cycle manufacturer, calculate the income under the head 'Profits and Gains of Business or Profession' for the year ending on 31st March.

	Rs.		Rs.
Salaries to employees	15,000	Gross Profit	80,000
Advertisement expenses	4,000	Interest on securities	4,000
General expenses	6,000	Income from house property	5,000
Entertainment expenses	2,000	Bad debts recovered (allowed earlier)	2,000
Bad debts	500		
Drawings by the proprietor	4,000		

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Sales-tax	1,000	
Interest on proprietor's capital	1,000	
Repairs	500	
Rent	1,000	
Legal expenses	5,000	
Depreciation	2,000	
Bonus (due)	3,000	
Bonus to the proprietor	1,000	
Car purchased	12,000	
Expenses on car during the year	2,000	
Donations	2,000	
Provisions for bad debts	2,000	
Net Profit	27,000	
	91,000	91,000

From the examination of books of accounts, the following other informations are available:

1. Out of advertisement expenses Rs. 1,000 were spent on neon signboards.
2. Rs. 1,000 were spent on purchase of land and are included in legal expenses.
3. Half of the repair expenses were on let-out building.
4. Depreciation allowable on all assets including car is Rs. 4,400.
5. Bonus was paid to employees on 30.6.97 and date of filing of return is 31.8.97.

Solution

Computation of business income of a cycle manufacturer.

		Rs.
Profit as given in the Profit and Loss A/c		27,000
Add: Inadmissible Expenses	Rs.	
Drawings	4,000	
Interest on proprietor's capital	1,000	
Bonus to proprietor	1,000	
Car purchased	12,000	
Donations	2,000	
Provisions for bad debts	2,000	
Legal charges (being Capital Exp.)	1,000	
Repairs on let-out building	250	
Depreciation	2,000	
		25,250
		52,250

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Less: Income to be treated under separate heads:		
Income from interest on securities	4,000	
Income from house property	5,000	
		9,000
		43,250
Less: Allowable depreciation		4,400
Income from business		38,850

Note : Bonus is allowed to be debited if it was paid before date of filing of return u/s 43 B.

Illustration 9. From the profit and loss account given below, calculate the taxable business income of the Partnership firm for the year ending on 31st March 1997 :

	Rs.		Rs.
Opening stock	1,60,000	Sales	8,00,000
Purchases	5,60,000	Commission	50,000
Wages	50,000	Interest	20,000
Salaries	40,000	Closing stock	1,80,000
Bad debts	1,500		
Rent	10,000		
Interest	10,000		
General charges	15,000		
Income-tax (firm's)	25,000		
Legal charges	8,000		
Insurance	2,500		
Conveyance	8,000		
Depreciation	30,000		
Bad debt reserve	5,000		
Net Profit	1,25,000		
	10,50,000		10,50,000

Following information was detected from the scrutiny of the accounts:

(*i*) Salaries include payment of salary to partners Alfa and Beta, Rs. 24,000 and Rs. 10,000 respectively.

(*ii*) Interest account includes payments made to partners on their capital at the rate of 16% p.a. as per terms of partnership deed: Alfa Rs. 2,000; Beta Rs. 2,500; Gama Rs. 2,500.

(*iii*) Rent includes rent paid to partner Gama Rs. 6,000.

(*iv*) Travelling expenses of Rs. 6,000 were spent on a tour to the U.K. by partner Gama to canvass for business, which are included in general charges.

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(*v*) Legal charges include: Penalty paid for violation of custom rules Rs. 4,500 partnership deed expenses Rs. 500.

(*vi*) General charges include a purchase of furniture of Rs. 3,000 and cash shortage of Rs. 200.

(*vii*) Half of the conveyance expenses are related to private use of the partners.

(*viii*) New machinery of Rs. 1,00,000 was installed during the year. The unit is engaged in the production of pesticides.

(*ix*) Allowable Depreciation on all assets including new P & M and Furniture amounts to Rs. 35,500.

(*x*) Mr. Alfa is working partner of the firm. As per partnership agreement he is entitled to salary as per above and a copy of deed was submitted to the assessing officer.

Solution

Computation of business income of the Partnership firm assessed as firm.

		Rs.
Profit as shown in the Profit and Loss A/c		1,25,000
Add: Inadmissible expenses	Rs.	
Income-tax	25,000	
Depreciation	30,000	
Bad Debts Reserve	5,000	
Salary to Partner Beta	10,000	
Salary to partner Alpha	24,000	
Legal charges regarding partnership deed (being capital expenditure)	500	
Penalty (it is not allowable deduction)	4,500	
Furniture purchased (being capital expenditure)	3,000	
Cash shortage (being capital loss)	200	
Conveyance Expenses (50% being personal expenses of partners)	4,000	
		1,06,200
		2,31,200
Less: Depreciation		35,500
Book Profit		1,95,700
Less: allowable remuneration u/s 40 (*b*)		24,000
Business Profit		171,700

Notes: 1. Rent paid to a partner is an allowable expenditure of the firm. Here Gama's building premises are used for the business of the firm.

2. Travelling expenses in connection with U.K. tour are allowed being in the interest of the business.

3. The penalty is disallowed.

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4. The payment of salary, to non-working partner is not allowed.
5. Interest on capital paid to partners is—allowed if it does not exceed 18% p.a.
6. Salary paid to working partner as per agreement is allowed u/s 40 (*b*).

Illustration 16. From the following statement, compute the income from profession of Dr. S.K. Kapoor.

	Rs.		Rs.
To Dispensary rent	6,000	By Visiting fees	15,000
,, Electricity and water charges	3,000	,, Consultation fees	25,000
,, Telephone expenses	2,000	,, Sales of medicines	12,000
,, Salary to nurse and compounder	6,000	,, Dividends	5,000
,, Dep. on surgical equipment	2,000		
,, Purchase of medicines	6,000		
,, Depreciation on X-ray Machine	1,000		
,, Income Tax	5,500		
,, Donation to Rama Krishna Mission	1,000		
,, Motor Car expenses	3,600		
,, Dep. on Car	1,800		
,, Net Income	19,100		
	57,000		57,000

Notes: 1. Electricity and water charges include domestic bill of Rs. 1,500.
2. Half of motor car expenses are for professional use.

Solution

Computation of Professional Income of Dr. S.K. Kapoor.

Professional Receipts	Rs.	Rs.
Visiting fees	15,000	
Consultation fees	25,000	
Sale of medicines	12,000	
		52,000
Less: Professional Expenses		
Dispensary rent	6,000	
Electricity and Water Charges (3,000 – 1,500)	1,500	
Telephone expenses	2,000	
Salary of staff	6,000	
Depreciation on surgical equipment	2,000	
Cost of medicines	6,000	

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Depreciation on X-ray Machine	1,000	
Motor Car expenses (3,600 – 1,800)	1,800	
Depreciation on Car (1,800 – 900)	900	
		27,200
Professional Gain		24,800

Illustration 11. The following is the Profit and Loss Account of a merchant for the year ending 31st March.

PROFIT AND LOSS ACCOUNT

	Rs.		Rs.
To Office Salary	6,500	By Gross Profit	36,750
,, Bad Debts written off	1,700	,, Commission	1,250
,, Provision for Bad Debts	3,000	,, Discounts	500
,, Advertisement	3,800	,, Sundry Receipts	200
,, Fire Insurance Premium (House Property)	550	,, Rent of Building	3,600
,, General Expenses	2,750	,, Profit on Sale of Investments	3,000
,, Depreciation	1,200		
,, Interest on Capital	2,000		
,, Interest on Bank Loan	1,300		
,, Net Profit	22,500		
	45,300		45,300

Compute the taxable profits from business. The amount of depreciation is Rs. 1,000.

Solution

Computation of Business Profits	Rs.	Rs.
Net profit as per P & L A/c		22,500
Add: Expenses not allowed		
Provision for Bad Debts	3,000	
Fire Insurance Premium	550	
Depreciation	1,200	
Interest on Capital	2,000	
		6,750
		29,250
Less: allowable depreciation		1,000
		28,250
Less: Incomes chargeable to tax under other heads:		
Rent of Building	3,600	
Profit on sale of investments	3,000	
		6,600
Business Income		21,650

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Illustration 12. Mr. D.D. Dewan & Company are Chartered Accountants in Delhi. They have submitted the following Income and Expenditure Account for the year. Compute the income from profession.

Expenses	Rs.	*Income*	Rs.
To Drawings	6,000	By Audit fees	24,000
,, Office rent	2,000	,, Financial Consultancy service	18,000
,, Telephone installation charges under O.Y.T. scheme	8,000	,, Dividends from an Indian company (Gross)	2,000
,, Electricity Bill	1,200	,, Dividend on units of U.T.I	1,000
,, Salary of Staff	6,000	,, Accountancy works	4,000
,, Charities	200		
,, Gifts given to relatives	5,600		
,, Scooter Expenses	1,000		
,, Subscription for Journals	500		
,, Institute fee	200		
,, Stipends given to trainees	1,200		
,, Net Income	17,100		
	49,000		49,000

Note. Depreciation during the year amounts to Rs. 500 only.

Solution

Computation of income from profession of M/s D.D. Dewan & Co.

Professional receipts	Rs.	Rs.
Audit fees	24,000	
Financial Consultancy works	18,000	
Accountancy works	4,000	
Gross Professional Receipts		46,000
Less: Professional Expenses		
Office rent	2,000	
Telephone Installation Charges	8,000	
Electricity Bill	1,200	
Salary of Staff	6,000	
Scooter Expenses	1,000	
Subscription for journal	500	
Institute fees	200	
Stipends to trainees	1,200	
Depreciation	500	
		20,600
Professional Gain		25,400

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Illustration 13. From the following particulars, compute the business income of Mr. S. Rangnathan.

	Rs.		Rs.
To Salaries	50,000	By Gross Profit	2,50,000
,, Rent and Taxes	10,000	,, Dividend	4,000
,, Service Charges	4,000	,, Bad debts recovered	
,, Legal expenses	5,000	(allowed earlier)	400
,, Reserve for Income-tax	3,000	,, Interest from Post	
,, Depreciation	8,000	Office Savings Bank	1,200
,, Expenses on acquisition of patent rights	7,000		
,, Office expenses	2,000		
,, Contribution to R.P.F.	1,200		
,, Bad Debts	1,500		
,, Donation to N.D.F.	2,500		
,, Net Profit	1,61,400		
Total	2,55,600	Total	2,55,600

Notes: 1. Legal expenses include Rs. 2,000 incurred by assessee for defending a case for damages for breach of contract which was decided in favour of assessee.

2. Depreciation of the year is Rs. 6,900.

Solution

Computation of business income of Mr. S. Ranganathan.

	Rs.	Rs.
Net profit as per Profit and Loss A/c		1,61,400
Add: Expenses claimed but not allowed		
Reserve for Income-tax	3,000	
Depreciation	8,000	
Patent rights	7,000	
Donation	2,500	
		20,500
		1,81,900
Less: Allowable expenses		
Depreciation	6,900	
Patent rights (1/14th of 7,000)	500	
		7,400
		1,74,500

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Less: Incomes not taxable under this head:		
Dividend	4,000	
Interest from Post Office Savings Bank	1,200	
		5,200
Business Profit		1,69,300

Notes: 1. Bad debts recovered but allowed earlier are taxable in the year in which they are recovered.

2. Interest on Post Office Savings Bank is exempted from tax.

Illustration 14. Given below is the Profit and Loss Account of Shri Durga Cotton Mills Ltd. for the year ended 31st March 1997 :

	Rs.		Rs.
To Opening Stock	5,50,000	By Sales	81,69,000
,, Purchases	55,60,000	,, Rent of Staff Quarters built in 1958	37,500
,, Railway Freight, Octroi etc.	6,00,000	,, Closing stock	8,49,500
,, Salaries and Wages	4,50,000		
,, Director's Fees	3,000		
,, Audit Fees (Paid in Cash)	25,000		
,, Legal Expenses	32,000		
,, Repairs to Building and Machinery	13,000		
,, Welfare Expenses	10,000		
,, General Charges	25,000		
,, Interest Paid	2,00,000		
,, Underwriting Commission for issue of share capital	10,000		
,, Reserve for Bad Debts	7,000		
,, Bad Debt written off	40,000		
,, Depreciation	10,000		
,, Managing Agent's remuneration	30,000		
,, Annual Contribution to Debenture Sinking Fund	25,000		
,, Provision for Taxation	5,00,000		
,, Contribution of Staff Welfare Fund	1,00,000		
,, General Reserve	1,00,000		
,, Proposed Dividends	6,00,000		
,, Balance to Balance Sheet	1,66,000		
Total	90,56,000	Total	90,56,000

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You are required to compute company's taxable income from business for the assessment year 1997-98 after taking into account the following information:

(*a*) A sum of Rs. 5,000 on account of liability foregone by a creditor has been carried to a special reserve. The said sum was charged by the company in the revenue account of the preceding year.

(*b*) General charges include—

(*i*) Rs. 7,000—Emergency Insurance Risk Premium.

(*ii*) Rs. 1,000—Donation to Chief Minister's Flood Relief Fund.

(*iii*) Rs. 2,000—Family Planning expenditure amongst company employees.

(*c*) Welfare expenses include Rs. 1,500 being cost of pucca well built for use by company workers.

(*d*) Legal expenses include Rs. 500 paid to a chartered accountant for conducting income-tax appeal and Rs. 2,000 (paid to an advocate) in connection with prosecution of Managing Agents for smuggling goods from Pakistan. The company made a profit of Rs. 20,000 on these smuggled goods.

(*e*) Repairs to Building include Rs. 10,000 being cost of additions to business premises.

(*f*) Depreciation (including additions to building) is Rs. 27,500.

[Calcutta University B.Com. (Hons.)]

Solution

Computation of Business Income

	Rs.	Rs.
Profit as per given in the P & L A/c		1,66,000
Add: Inadmissible deductions		
Reserve for Bad debts	7,000	
Depreciation	10,000	
Annual Contribution to Debenture Sinking Fund	25,000	
Provision for Taxation	5,00,000	
General Reserve	1,00,000	
Proposed dividend	6,00,000	
Staff Welfare Fund	1,00,000	
Liability forgone by creditor	5,000	
Donation to Flood Relief Fund	1,000	
Expenses on the construction of pucca well (being capital expenditure)	1,500	
Legal expenses being expenses incurred against the prosecution of managing agents	2,000	
Cost of addition to business building (being capital expenditure)	10,000	

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Underwriting Commission—		
9/10th of Rs. 10,000	9,000	
Audit fees [being paid in cash: disallowed u/s 40 A (3) upto 20%]	5,000	
		13,75,500
		15,41,500
Less: Allowable depreciation		27,500
		15,14,000
Add: Other Business Incomes;		
Income from smuggling business	20,000	
Less: Expenses incidental to smuggling business	2,000	
		18,000
Company's Business Income		15,32,000

Notes: 1. Rent received from employee's quarters is incidental to company's business and hence it is a business income.

2. Emergency insurance risk premium is incidental to business.
3. Expenditure on family planning is an allowable deduction in case of company assessee.
4. Commission on underwriting shares is preliminary expenditure and u/s 35D 1/10th is allowed every year.
5. Legal expenses on appeal against tax authorities decision are allowed.
6. Contribution to staff welfare fund is disallowed.
7. Since the payment made in cash exceeds Rs. 20,000 hence 20% of such payment is disallowed.

Q. No. 5

Discuss the admissibility of following items under the head Profits and Gains :

(*a*) Mr. X has received a notice from Sales Tax authorities and he created a reserve for Rs. 6,000 on 31.3.97. He paid Rs. 3,000 on 14.8.97 and Rs. 3,000 on 1.10.97 He filed his return on 31.8.97.

(*b*) Mr. R declared a bonus of Rs. 1,00,000 for employees but due to paucity of funds he could pay Rs. 40,000 on 31.3.97, Rs. 30,000 on 30.10.97 and balance on 21.11.97. Due date for filing of his return is 31.10.97.

(*c*) A payment of Rs. 42,000 by cheque as employers' contribution to provident fund, made on 30.11.96, due date being 15.12.96. The cheque was realised on 31.12.96.

[**Hints :** (*a*)Rs. 3,000 allowed during assessment year 1997-98 and Rs. 3,000 during assessment year 1998-99 ;

(*b*) Rs. 70,000 allowed during assessment year 1997-98 and Rs. 30,000 during 1998-99;

(*c*) Payment of Rs. 42,000 will not be allowed in any of the previous year as cheque was not realised within 15 days.]

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Q. No. 6

To what extent following are allowed as deductions in computing the income of business carried on by A:

(*i*) Entertainment expenditure incurred during the previous year ending 31.3.1997 is Rs. 50,000.

(*ii*) Daily allowance given to Mr. Mohan, an employee is at the rate of Rs. 2,000 per day. He was on tour for 5 days and was given Rs. 10,000 as daily allowance during previous year 1996-97.

(*iii*) Ten items were presented during previous year 1996-97 on advertisement each costing Rs. 2,000.

(*iv*) Income-tax deposited in advance during the previous year 1996-97 amounted to Rs. 10,000.

[Punjab University B. Com. Oct. 1995]

[**Hints :** (*i*) Allowed Rs. 30,000 (*ii*) Allowed Rs. 9,375 (*iii*) Allowed upto Rs. 15,000 (*iv*) Disallowed].

Q. No. 7

The following is the Profit and Loss Account of Mr. Roy for the year.

	Rs.		Rs.
To Rates and Taxes	450	By Gross Profit	14,623
,, Establishment (Staff)	1,750	,, Bank Interest on	
,, Rent	600	personal deposits	577
,, Household expenses	1,450		
,, Discount	250		
,, Advertisement	200		
,, Income-tax	480		
,, Postage, Stationary	810		
,, Fire Insurance	150		
,, Gift and Presents	160		
,, Charity and Donations (to approved institutions)	1,140		
,, Purchase of Plant and Machinery (not yet installed)	1,500		
,, Repairs of furniture	50		
,, Interest on loan	1,000		
,, Life insurance premium	600		
,, Reserve for Doubtful debts	700		
,, Interest on capital	250		
,, Net profit	3,660		
	15,200		15,200

You are required to ascertain the business income of Shri Roy.

[P.U. Cal. University B. Com.]

[**Hints:** Business Income Rs. 9,363]

Q. No. 8

Ram Prasad is a registered medical practitioner. He has prepared the following Income and Expenditure Account for the year during 31st March, 1997. You are required to prepare a statement showing his income from profession.

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INCOME AND EXPENDITURE ACCOUNT

	Rs.		Rs.
Household Expenses	20,000	Consultation fees	10,000
Car purchased	30,000	Visiting fees	20,000
Travelling Expenses (personal)	4,000	Gains on Race (gross)	10,000
Charity & Donations	1,000	Share in sale proceeds of an ancestral house	34,000
Income Tax	2,000	Profit on sale of securities	6,000
Salaries	8,000	Dividend on shares (gross)	5,000
Gift to daughter	7,000	Interest on P.O. Savings Bank	600
Establishment Exp.	1,000	Gifts from Father-in-Law	2,000
Surgical Equipment	4,000	Bad debts recovered (Not allowed in earlier year)	2,000
Books	1,200	Interest on fixed deposit	1,300
Life Insurance premium	2,000		
Wealth-Tax	1,000		
Interest on Capital	1,000		
Surplus	8,700		
	90,900		90,900

Rate of Depreciation allowable on car is 20% and surgical equipments is at 25%. In case of books for profession in rate of depreciation is 100%.

[Nagarjuna B. Com. April, 1995]

[Hints : Professional gain Rs. 12,800]

Q. No. 9

Mr. X is the owner of a business. He has submitted the Profit and Loss Account prepared for the year ending on 31.3.1997. You are required to compute the business income of Mr. X for the assessment year 1997-98.

PROFIT AND LOSS ACCOUNT

	Rs.		Rs.
To Salary to proprietor	10,000	By G.P. b/d	50,000
,, Staff salary	15,000	,, Profit on sale of car (Capital Gain)	15,000
,, General expenses	7,000	,, Bad debts recovered	5,000
,, Interest on capital	2,000	,, Interest on Govt. Securities (Gross)	4,000
,, Bad debts	1,000	,, Dividends (Gross)	4,000
,, Advertisements	2,700	,, Interest on Post Office savings A/c	4,000
,, Fire Insurance	1,000		
,, Depreciation	3,000		
,, Provision for doubtful debts	1,000		
,, Income-tax	4,000		
,, Donation to a school	3,000		
,, Car expenses	3,000		
,, Net profit	29,300		
	82,000		82,000

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Additional Information:

1. Depreciation as per income-tax rules is Rs. 2,500 only.
2. General expenses include Rs. 500 spent on printing of calenders.
3. Advertisement include cost of neon signboard costing Rs. 1,000.

[**Hints:** Business Profit Rs. 22,800]

Q. No. 10

The net profit disclosed by the Profit and Loss Account of D. Sen, owning a Departmental Store, for the year ended 31st March, 1997 is Rs. 20,000. The undernoted particulars and information are available in regard to the accounts:

(*a*) Stock of goods as at 1.4.96 and 31.3.97 has been valued at Rs. 2,50,000 and Rs. 3,00,000 at 20% below cost, the market values being Rs. 3,50,000 and Rs. 4,20,000 respectively.

(*b*) Mr. Sen withdrew from the trading stock for his domestic use goods which had cost Rs. 10,000 and credited to sales by a sum of Rs. 5,000 debiting his capital account. The market value of the goods on the date of withdrawal was Rs. 15,000.

(*c*) Articles of foreign manufacture were imported infringing the Customs Regulations and penalty of Rs. 10,000 paid and the amount was debited to the Profit and Loss Account under 'Legal Expenses'.

(*d*) 'Legal Expenses' also include cost of stamp duties and mortgage charges of Rs. 8,000 for giving security of immovable properties against a long-term business loan of Rs. 5,00,000 taken from the I.C.I.C.I.

(*e*) Depreciation debited to accounts falls short of the admissible depreciation for taxation purposes by Rs. 25,000.

(*f*) Shares acquired for investment purposes on 1st October, 1994 at a cost of Rs. 35,000 were sold on 31st December, 1996 for Rs. 60,000. Gain has not been credited to P & L A/c.

(*g*) Machinery hired by D for use in his business was destroyed by fire and compensation of Rs. 10,000 paid to the owner on that account was debited to the Profit and Loss Account.

From the information given above, compute business income of Mr. Sen for the assessment year 1997-98.

[**Hints:** Hired machinery loss is a business loss, P & L A/c under credited Rs. 75,000 under debited is Rs. 62,500. Business profit Rs. 22,500, Profit on shares is Capital gains] [P-14].

Q. No. 11

Mr. Surajmal is carrying on agency business. From the following information compute his Income from business for the Assessment year 1997-98 :

(*i*) Commission earned—
  (*a*) @ 6% on total sales of Rs. 4,00,000 from Hindustan Lever Ltd.
  (*b*) @ 5% on total sales of Rs. 3,00,000 from Brooke Bond India.
  (*c*) @ 4% on total sales of Rs. 2,00,000 from Glaxo company.
  (*d*) @ 7% on total sales of Rs. 5,00,000 from Proctor and Gamble.

(*ii*) Compensation received from Tata Oil for termination of their agency Rs. 40,000.

(*iii*) Commission received from Godrej Co., @ 8% on total sales of Rs. 1,25,000. He paid compensation to Bhat and Sons, Sirsi Rs. 10,000 for getting some modification in the terms of agency agreement with them.

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The following expenses have been incurred:

Rent of the building Rs. 16,000. Salary to Staff Rs. 15,000. Advertisement Rs. 25,000. Printing and Stationery Rs. 12,000. Wages to labourers Rs. 11,000. Income-tax paid Rs. 10,000. Income-tax Appeal expenses Rs. 3,000. Miscellaneous expenses. Rs. 14,000. Half of the building is used by him as his residence

[Karnataka B.Com. 1994]

[**Hints :** Business incomes Rs. 34,000; Compensation received is revenue receipt and compensation paid is revenue expenditure]

Q. No. 12

Following is the Profit and Loss Account of Kesari Malya for the previous year 1996-97.

PROFIT AND LOSS ACCOUNT

	Rs.		Rs.
To Salaries	25,650	By Gross profit	80,000
,, Rent	1,000	,, Bank interest	450
,, Commission on sales	100	,, Bad Debts recovered (last year allowed)	2,000
,, Income-tax	2,600	,, Rent from house property	4,800
,, Entertainment expenses	600	,, Interest on commercial securities	2,000
,, Commission paid to collect interest on securities	25		
,, Embezzlement by cashier	1,000		
,, Municipal tax of H.P.	600		
,, Bad Debts (allowed)	450		
,, Repairs to house	1,625		
,, Office expenses	9,180		
,, Depreciation	5,000		
,, L.I.C. premium	1,320		
,, Net profit	40,100		
	89,250		89,250

(*a*) Depreciation on the assets is Rs. 4,500.

(*b*) Construction of the let-out house was completed in 1988.

Compute the taxable Business income for the Assessment year 1997-98.

[**Hints:** Business profit Rs. 39,520]

Q. No. 13

Mr. Mahalingam furnishes the following particulars. Compute his income from business for the assessment year 1997-98 :

(*a*) Legal expenses to the extent of Rs. 5,000 represent the amount spent for curing the defect in the title of business asset and balance amount on acquiring the asset.

(*b*) Know-how was developed in a laboratory financed by the State Government.

(*c*) Actual bad debts amounted to Rs. 3,000 only.

(*d*) Advertisement expenditure was paid in cash.

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Profit and Loss Account for the year ended March 31, 1997

	Rs.		Rs.
Trade expenses	1,500	Gross profit	1,00,000
Wages and salaries	33,000	Refund of income tax penalty levied earlier	22,150
Advertisement expenses	20,000		
Income tax	7,500		
Contribution to staff welfare fund	1,000		
Donation to Prime Minister's National Relief Fund	2,000		
Life insurance premium on own life	750		
Provision for doubtful debts	5,000		
Interest on capital	3,550		
Provision for sales tax	2,500		
Expenditure on know how	18,000		
Wealth tax	5,000		
Gift tax	1,500		
Gifts to 20 customers	2,000		
Fire Insurance Premium	850		
Legal Expenses	8,000		
Net Profit	10,000		
	1,22,150		1,22,150

[B.Com. Madurai, Oct. 1994]

[**Hints** : Legal expenses on curing title of business assets disallowed ; Technical know how 1/3rd allowed; Advertising expenditure disallowed; Business Profit Rs. 53,650.]

Q. No. 14

Following is the Profit and Loss Account of a Merchant.

	Rs.		Rs.
To Rent	6,000	By Gross Profit	52,300
,, Rates	600	,, Interest from Debtors	2,800
,, Salary of Staff	5,400	,, Rent from Property	2,400
,, Diwali Pujan Expenses	200	,, Sundry Income	1,600
,, Interest on Loan	12,500	,, Commission	3,700
,, Sundry Expenses	5,500		
,, Bad Debts	600		
,, Charity	100		
,, Reserve for Bad Debts	200		
,, Entertainment	850		

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To Loss by theft	1,400		
,, Net Profit	29,450		
	62,800		62,800

Notes: (*a*) Rent includes Rs. 1,200 of a shop belonging to the assessee himself.

(*b*) Salary of staff includes salary of Rs. 2,400 of a son, who is a B. Com. student and who casually helps in the business.

(*c*) A loan of Rs. 6,000 @ 15 per cent p.a. is taken from his wife out of funds advanced by him.

(*d*) Sundry Expenses include Rs. 900 being expenses incurred on pilgrimage to Hardwar.

(*e*) Entertainment includes Rs. 150 spent on tea of some guests of a local M.L.A.

(*f*) Loss by theft took place when a pretended customer stole a necklace worth Rs. 600; Rs. 800 were stolen from his house in the night by de-locking.

(*g*) He earned Rs. 4,000 in gold smuggling not shown in books.

(*h*) Rates include Rs. 400 for the property let.

Compute the merchant's Business Income.

[Adapted I.C.W.A. Final]

[**Hints:** Business Income Rs. 34,100. Smuggling Business Income Rs. 4,000, Loss by theft from house, Salary to son, Hardwar expenses, entertainment expenses of M.L.A. are not allowed. Smuggling income is business income, Loss due to theft by a pretended customer is allowable]. [P-2].

Q. No. 15

The following is the P & L A/c of Robert on the basis of which compute his gross total income for the assessment year 1997-98 :

	Rs.		Rs.
Salaries and wages	12,000	Gross Profit	48,200
Rent Rates Taxes	3,200		
Trade expenses	1,450	Rent from House property	6,000
Advertisements	950		
Household expenses	3,500	Dividend from an Indian company	2,400
Discount & rebate	1,250		
Postage & Stationary	275		
Fire Insurance Premium (Letout house property)	300		
Reserve for bad debts	1,000		
LIC Premium	1,000		
Donation to an approved school	1,000		
Income Tax	3,300		
Repairs (House Property)	500		

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Audit fees	300	
Loss of stock in trade	1,000	
Depreciation	1,000	
Interest on capital	200	
Net profit	24,375	
	56,600	55,600

Additional information : 1. Depreciation allowable is Rs. 500.

2. He owns another house which is self occupied and for which he has paid Rs. 12,000 as interest on loan taken for its repairs.

[Hints : Profit and Gains Rs. 27,275 ; H/Property loss to be set off Rs. 5,500 ; other sources Rs. 2,400 G.T.I. Rs. 24,175]

Q. No. 16

Following is the Profit & Loss Account for the year ended 31st March, 1997 of Mr. S. Saha, a sole trader.

	Rs.		Rs.
To Opening Stock	80,000	By Sales	12,00,000
,, Purchases	9,20,000	,, Closing stock	90,000
,, Gross profit c/d	2,90,000		
	12,90,000		12,90,000
,, Salaries	55,000	To Gross Profit b/d	2,90,000
,, Rent	25,000	,, Bank interest	500
,, Commission	5,000		
,, Legal charges	4,500		
,, Bad debts written off	14,500		
,, Reserve for bad debts	11,500		
,, Repairs to machinery	1,500		
,, Depreciation on fixed assets	26,500		
,, Other expenses	2,000		
,, Income Tax	20,000		
,, Net Profit	1,25,000		
	2,90,500		2,90,500

Compute income under the head 'Profits and Gains of Business or Profession' of Mr. Saha for the assessment year 1997-98 after taking into consideration the following information:

(*a*) Sales include the value of goods worth Rs. 50,000 which were drawn by Mr. Saha for his personal use. The cost price of such goods on the date of transfer was valued at Rs. 45,000 and their market price was valued at Rs. 56,000.

(*b*) Rent includes Rs. 3,600 which was charged by Mr. Saha, relates to the house which was used as part of his own residence.

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(c) Bad debts include Rs. 3,000 which were not finally settled as irrecoverable, but the same were included in the last year's sales.

(d) Legal charges include Rs. 500, the fees paid for the registration of the title deeds of a land acquired for the business last year.

(e) Depreciation allowable as per Income-tax rules for the year was Rs. 30,000.

(f) Both opening and closing stocks of the year were undervalued at 20% below cost.

[Calcutta University B.Com. (Hons.) 1982]

[Hints: Sales to be decreased by Rs. 50,000; and Rs. 45,000 to be treated as drawings. Business Profit Rs. 1,57,100] [P-5].

Q. No. 17

Mr. Kedambi, an Advocate, furnishes the following receipts and payments for the previous year 1996-97:

RECEIPTS AND PAYMENTS A/c

	Rs.		Rs.
To Balance b/d	6,540	By Rent	2,400
,, Legal Fees	84,400	,, Telephone	3,000
,, Salary (as a part-time law lecturer)	3,600	,, Salaries	2,400
,, Interest on debentures (Not-listed)	2,700	,, Subscription to Law Journal	240
,, Gift from clients	10,000	,, Travelling	560
,, Rent	6,000	,, Office expenses	600
,, Interest on foreign security	8,000	,, Purchase of stamp paper and court fee stamps	1,600
,, Refund from Compulsory Deposit	2,000	,, Interest on loan	870
		,, Donation to a school	5,000
		,, Income Tax paid	8,420
		,, Municipal Tax	600
		,, L.I.C. premium	6,000
		,, Wealth Tax	1,600
		,, Balance c/d	89,950
	1,23,240		1,23,240

(a) The loan was borrowed for constructing his residential house. Its rental value is Rs. 300 per month.

(b) School is recognised for I.T. purposes.

(c) Gift from clients includes Rs. 2,000 received from his father.

Compute the Professional Income. *[B.Com. Mysore]*

[Hints: Professional Gain Rs. 81,600]

Q. No. 18

The following is the Profit and Loss Account of Mr. X for the year ended on 31.3.1997. Compute his taxable Business income for the year.

	Rs.		Rs.
To Opening Stock	15,000	By Sales	80,000
,, Purchases	40,000	,, Closing Stock	20,000
,, Wages	20,000	,, Gift from Father	18,000

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To Rent	6,000	,, Sale of Motor Car	9,000
,, Repair to Motor Car	3,000	,, Income Tax Refund	3,000
,, Wealth Tax Paid	2,000		
,, Medical Expenses	3,000		
,, General Expenses	10,000		
,, Depreciation on Motor Car	4,000		
,, Advance Income Tax paid	1,000		
,, Profit for the year	26,000		
	1,30,000		1,30,000

Following further information is given:

1. Mr. X carries on his business from rented premises at Delhi, half of which is used as his residence.
2. Mr. X bought a car during the year for Rs. 20,000. He charged depreciation on the value of the car. The car was sold during the year for Rs. 9,000. The use of the car was 3/4th for the business and 1/4th for personal purposes.
3. Medical expenses were incurred during sickness of Mr. X for his treatment.
4. Wages include Rs. 250 per month on account of Mr. X's driver for 10 months. *[C.A. (Inter)]*

[**Hints:** Business Income 10,375; Loss on sale of car is short term capital loss] [P-10].

Q. No. 19

Shri R.K. Nair is a leading lawyer of Mysore. He deposits all receipts in the bank and pays all expenses by cheque. Following is the analysis of his bank account for the year ending 31st March 1997:

	Rs.		Rs.
Balance b/d	7,887	Salaries	14,000
Professional Income	1,40,000	Rent of Chamber	4,500
Dividend (Gross Rs. 10,000)	8,000	Telephone expenses	1,000
House rent	22,500	Professional expenses	3,000
Race course income	9,000	Motor Car expenses	8,000
Share of income from H.U.F.	5,113	Miscellaneous office expenses	5,500
		Dep. on Car	3,000
		Advance Income-tax	40,000
		Donation to Mysore University	10,000
		Personal expenses	45,500
		House Property expenses	
		Municipal tax	5,000
		Repairs	1,500
		Insurance	1,500
		Collection charges	2,000
		Balance c/d	48,000
	1,92,500		1,92,500

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Compute Shri Nair's professional income after taking into account the following:

(*a*) 1/4th of the Motor Car expenses relate to personal use.

(*b*) Shri Nair stays in house, the Municipal value of which is Rs. 9,800. Following are the expenses which have been included in the above account in respect of this house:

Insurance premium	Rs. 500
Municipal tax	Rs. 2,400

[Mysore B.Com.]

[Hints: Professional Income 1,03,750] [P-12].

Q. No. 20

G. Ganesan has prepared the following Profit and Loss Account for the year ending March 31, 1997:

	Rs.		Rs.
Salaries	8,000	Gross Profit	30,800
Advertisement	4,000	Rental Income (50% portion)	18,000
Sundry expenses	4,500	Dividends from an Indian company (gross)	4,000
Interest on capital	2,000	Winning from lottery (gross)	20,000
Fire Insurance (Rs. 1,000 relates to house property)	3,000	Interest on Govt. securities	2,000
Income-tax and Wealth-tax	7,000		
Household expenses	2,500		
Bad Debts	1,000		
Provisions of bad debts	500		
Repairs of house property	1,000		
Municipal taxes of house property	3,600		
Insurance premium on own life	6,000		
Donation to Prime Minister's Relief Fund	2,000		
Depreciation	3,700		
Net Profit	26,000		
	74,800		74,800

Ganesan owns a house property which is being used by him for the following purposes:

(*a*) 25% of the carpet area for his own business purposes.

(*b*) 25% of the carpet area for the purpose of self-residence.

(*c*) 50% of the carpet area is let out for residential purposes.

Compute the business profit of Ganesan for the assessment year 1997-98

[Hints: Net Business Profit Rs. 6,200] [P-13].

Q. No. 21

From the following Trading and Profit and Loss Account of Mr. B for the year ended 31st March, 1997, compute his business income.

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	Rs.		Rs.
To Opening Stock	32,000	By Sales	4,20,000
,, Purchases	3,60,000	,, Closing Stock	48,000
,, Gross Profit	76,000		
	4,68,000		4,68,000
,, Salaries and Wages	36,400	,, Gross Profit	76,000
,, Rent paid	10,800	,, Dividends received	
,, Insurance Premium	2,890	from Indian Companies (Tax deducted	
,, Printing and Stationery Advertisement Expenses	1,700 720	at source Rs. 800)	3,200
,, B's Household Expenses	26,000		
,, Net Profit	690		
	79,200		79,200

As analysis of the expenses revealed the following:

(*a*) Salaries and wages includes Rs. 18,000 charged as salary to B and Rs. 400 paid to B's domestic servant.

(*b*) Rent included Rs. 1,800 being hostel charges of B's minor son.

(*c*) Rs. 1,600 paid as Life Insurance Premium on a policy on Mrs. B's life was included in Insurance Premium.

(*d*) B also owns a house property which had been fully let out at Rs. 800 p.m. Municipal taxes of Rs. 2,100 paid annually on this property had been included under household expenses.

(*e*) Household expenses also includes Rs. 3,800 being the amount paid into a public provident fund account in B's name.

[**Hints:** Business Income Rs. 45,290] [P-4].

Q. No. 22

Indian Trading Co., a proprietary business of Shri. J.M. Banerji a resident individual, shows a net profit of Rs. 30,600 for the year ending on 31st March. On scrutiny the following position is revealed:

(*a*) The assessee has under-valued both opening and closing stock at 5%. Book values of the stocks are Rs. 57,000 and Rs. 76,000 respectively.

(*b*) Taxes include pleader's fees for a criminal appeal case Rs. 600.

(*c*) Depreciation over-charged in the accounts by Rs. 3,000.

(*d*) Proprietor's drawing accounted for in the Misc. expenses A/c Rs. 5,000 and Life Insurance Premium of Rs. 1,500 on own life policy debited to Insurance A/c.

(*e*) Investment allowance of Rs. 2,000 charged to P & L A/c without depositing it with Development Bank.

(*f*) The assessee has contributed to P.P.F. A/c Rs. 2,200 out of his drawings.

(*g*) The personal A/c of Sh. J.M. Banerji shows a credit of Rs. 2,200 which he explains as a share of profit from a joint venture business and claims it as exemption as a casual gain as business was casually carried on in the year and did not continue.

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Compute the business income stating your reasons wherever necessary.

[Calcutta University (adapted) B.Com. (Hons.)]

[**Hints:** Profit from Bharat Trading Co. Rs. 43,700, Profit from joint venture Rs. 2,200] [P-6].

Q. No. 23

The following is the P & L A/c for the year ended 31st March 1997 of the Bengal Sugar Mills of which X is the owner:

PROFIT AND LOSS ACCOUNT

	Rs.		Rs.
To Manufacturing Exp.	5,85,295	By Sale of Sugar and Molasses	11,61,300
,, Excise duty	2,07,500	,, Rent from Agricultural lands	950
,, Salary & Wages	1,00,495	,, Revenue from Fisheries	3,700
,, Establishment Charges	50,150	,, Sale Proceeds of agri. produce	6,07,355
,, General Charges	33,750	,, Sundry Receipts	1,230
,, Fine paid to Excise Dept.	1,750		
,, Interest on Bank loans	24,000		
,, X's remuneration	41,000		
,, Depreciation	69,000		
,, Cultivation Expenses	4,57,500		
,, Income-tax	25,000		
,, Net Profit	1,79,095		
	17,74,535		17,74,535

Compute the business income of Mr. X after taking the following informations in consideration:

(*i*) Manufacturing Expenses include Rs. 5,12,000 on account of cane produced in own farms and consumed in the factory and debited to manufacturing expenses, the average market price of such cane being Rs. 5,75,000.

(*ii*) General charges include (*a*) Rs. 1,000 as legal expenses incurred in defending a suit regarding the company's title to certain agricultural lands, and (*b*) Rs. 9,000 paid to Shri X's son who is an employee in the Sugar Mill for a trip to Hawaii to study modern methods of manufacture.

(*iii*) Depreciation in respect of all assets has been calculated as Rs. 75,000.

[C.U., B.Com. (Hons.)]

[**Hints:** Sugar Mill Profit Rs. 24,340 Rent from agricultural land and Sale Proceeds of canes all exempted being agricultural income. Difference between market price of cane crushed and amount actually charged is also agricultural income. Revenue from fisheries is income from other sources. Expenses on Trip to Hawaii is an allowable expenses of Business, legal expenses on agri. land disallowed] [P-7].

Q. No. 24

The Profit and Loss Account for the year ended 31st March 1997 of Arun and Sons, proprietary concern is as follows:

Dr.	Rs.	Cr.	Rs.
To Opening stock	50,000	By Sales	19,40,000
Purchases	12,00,000	,, Closing Stock	60,000

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To Wages	3,00,000	
,, Salaries	1,00,000	
,, Interest	45,000	
,, Customs duty	12,000	
,, General charges	63,000	
,, Depreciation	53,000	
,, Income-tax	55,000	
,, Net profit	1,22,000	
	20,00,000	20,00,000

The following particulars are available:

(*i*) Both the opening and closing stocks are valued 20% under cost.

(*ii*) 'Wages' include a sum of Rs. 5,000 paid to the proprietor's domestic servants.

(*iii*) 'Interest' includes Rs. 10,000 (for the period 1.5.95 to 31.7.96) paid in respect of a loan taken to purchase a machine which was installed on 1st August, 1996.

(*iv*) 'Customs duty' includes Rs. 4,000 for clearing the machine referred to in (*iii*).

(*v*) Depreciation debited represents the amount admissible for income-tax purposes.

(*vi*) Compute the Business income of the proprietor on the basis of the above-noted data giving your reasons wherever necessary.

[C.U., B.Com. (Hons.)

[**Hints:** Business Profit 1,98,500. Interest for the period prior to installation and customs duty on clearing of machine are capital expenses]

Q. No. 25

Prakash is a small businessman. He gives you the following details drawn from his books of accounts, for the year ending 31-3-97.

(*i*) Computed net profit after charging the following Rs. 55,000.

(*ii*) Provisions and reserves debited to profit and loss account.

(*a*) Provisions for doubtful debts	30,000
(*b*) Depreciation reserve	40,000

(*iii*) Household expenses 60,000

(*iv*) Donation to Prime Minister's National Relief Fund Rs. 20,000; other charitable donations Rs. 40,000.

(*v*) Cheques issued for purchases Rs. 20,000.

(*vi*) O.Y.T. Deposit Rs. 10,000.

(*vii*) Advertisement expenses Rs. 5,000 spent on a signboard given to a customer; advertisement gifts to fifty customers at a cost of Rs. 100 each.

(*viii*) Audit fees Rs. 20,000.

(*ix*) Patents purchased for Rs. 70,000 during the previous year.

(*x*) Market survey expenses Rs. 8,000, Feasibility Report Expenses Rs. 12,000 on a new project of Rs. 10,00,000.

(*xi*) Incomes credited to profit and loss account were:

(*a*) Bank Interest on FD	Rs. 5,000
(*b*) Interest on Post Office Savings Bank A/c	Rs. 3,000
(*c*) Interest on UTI units	Rs. 2,000

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(*xii*) Opening Stock is valued at cost + 10% basis where as closing stock is valued at cost – 10% basis. Opening stock valued was Rs. 1,32,000 and closing stock was valued Rs. 1,44,000.

Compute the net business income for the Assessment year 1997-98.

[**Hints :** Business Income Rs. 3,46,000; difference due to valuation of stock Rs. 12,000 + 16,000 to be added; preliminary exp. to be disallowed Rs. 18,000 (9/10); Patent rights to be disallowed Rs. 65,000 (13/14)]

Q. No. 26

The following is the Profit & Loss Account of Sri S. Kumar for the year ending 31st March, 1997:

	Rs.		Rs.
To Rent	3,870	By Gross Profit b/d	48,748
,, Staff Salaries	8,620	,, Misc. Receipts	383
,, General Charges	3,780	,, Discounts	458
,, Int. on Capital	1,800	,, Interest on Govt. Securities	2,400
,, Int. on Bank Loan	750	,, Bad Debts recovered	560
,, Audit Fee	300	,, Profit on Sale of Investments	5,765
,, Bad Debt	840		
,, Reserve for Bad Debt	600		
,, Income Tax	2,400		
,, Law Charges	3,700		
,, Compensation to a retrenched employee	2,800		
,, Cost of extension of office premises	2,000		
,, Charity and Donation	184		
,, Depreciation	5,700		
,, Entertainment expenses	6,300		
,, Net Profit	14,670		
	58,314		58,314

Compute Mr. Kumar's income from business for the relevant assessment year after taking into account the following:

(*a*) The expenditure of rent includes a sum of Rs. 720 being rent charged for a godown owned by the assessee himself.

(*b*) Staff salary includes Rs. 1,200 being the salary of a servant engaged at the residence of the assessee.

(*c*) The general expenses includes a sum of Rs. 500 being the cost of a Neon signboard.

(*d*) Claim for Bad Debt includes an item of Rs. 300 due from Mr. Y, since 5.8.1994 who is insolvent.

(*e*) Law Charges includes payment of Rs. 2,000 being Stamp, Registration and Solicitor's Bill for the Deed of purchase of a property.

(*f*) Depreciation on fixed assets according to Income-tax Rules amount to Rs. 6,780.

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(g) Bad Debts recovered includes an item of Rs. 200 the claim for which was disallowed in the related year of assessment. *[C.U., B.Com. (Hons.)]*

[Hints: Business Income Rs. 16,129 retrenchment compensation is allowed].

Q. No. 27

Mr. G.R. Sharma carries on his own business as Chemist. For the year ending March 31, 1997, Trading/Profit and Loss Account was as follows:

	Rs.		Rs.
To Opening Stock	20,000	By Sales	1,27,000
,, Purchases	1,09,000	,, Closing Stock	52,000
,, Salaries	6,000	,, Interest on Reliance Co. Ltd. Debentures	2,000
,, Rent	11,000	By Dividend	2,000
To Bonus	3,000	,, Discount Received	12,000
,, Printing, Postage and Stationery	4,000	,, Race Winnings	12,000
,, Miscellaneous Expenses	4,000	,, amount received from LIC on maturity of policy	15,000
,, Advertisement Expenses	5,000	,, Share of Profits in Association of persons	30,000
,, Drawings	12,000		
,, LIC Premium	5,000		
,, Car Expenses—			
Driver's Salary	6,000		
Petrol, Repairs	12,000		
,, Property Tax	4,000		
,, Medical Expenses of physically handicapped son at Holy Family Hospital	3,000		
,, Cost of National Savings Certificate (Series VIII)	3,000		
,, Net Profit	45,000		
	2,52,000		2,52,000

Additional information is as follows:

Advertisement expenses included cost of 20 gift sets of Rs. 250 each presented to doctors on occasion of Diwali.

Assume:

Taxes deducted at source on Dividends and Debentures are 'Nil'.

The car was used both for business and personal purposes, 2/3rd is for business.

Property Tax of Rs. 4,000 was in respect of his self-occupied house whose Rental value is Rs. 18,000.

Compute the Business Income of Mr. Sharma for the assessment year 1997-98.

[C.A. Inter, May 1986]

[Hints: Advertisement expenses allowed. Income from chemist business Rs. 17,000, share from an association of persons Rs. 30,000. Income under head 'Profits and Gains' Rs. 47,000] [P-17]

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Q. No. 28

A HUF carrying on business in gold, silver, money lending, brokerage and security dealings showed the following particulars in a statement filed for the previous year ending on 31st March, 1997 :

	Rs.		Rs.
Loss in silver	50,000	Profit in gold	2,00,000
Loss on sale of securities	60,000	Income from Money lending business	50,000
Loss in share dealings	40,000	Income from Brokerage	30,000
Legal charges	10,000	Interest on securities (Gross)	80,000
Bad debts	30,000	Dividends from Indian Companies	96,000
Life Insurance premium paid on the life of karta	5,000	Amount received from Life Insurance Corporation on Maturity of a policy of karta	20,000
Donation to Indira Gandhi Memorial Trust	5,000	Winning from lottery	4,000
Establishment Charges	20,000		
Sales Tax	4,000		
Purchase of Scooter for the business	16,000		
Drawings	20,000		
Net Profit	2,20,000		
	4,80,000		4,80,000

On inquiry and examination the following further information was obtained:

(*a*) A loss of Rs. 40,000 in hedging contract and a loss of Rs. 60,000 in speculation were found debited in Silver Account.

(*b*) Legal charges included expenses of Rs. 2,000 incurred in a criminal case connected with alleged purchase of smuggled gold.

(*c*) Bad debts included loss of cash Rs. 5,000 by theft during night from safe box of the business premises and Rs. 10,000 as an irrecoverable loan given without interest to his brother-in-law, whose business failed.

(*d*) Establishment charges included salary of Rs. 10,000 paid to the son of karta who actually helped in the business. Compute business income of HUF.

[B.Com. P.U. April 1988]

[**Hints:** Business income Rs. 1,34,000; Hedging loss and loss due to theft during night are allowed; LIC Maturity amount is exempted. Dep. on Scooter @ 25%] [P-18].

Q. No. 29

Following is the P & L A/c of Mr. A.

	Rs.		Rs.
To Salary	30,000	By Gross Profit	2,35,000
„ Depreciation	25,000	„ Sundry Receipts	66,200
„ Office Expenses	18,000		
„ Travelling Expenses	10,000		
„ Expenditure on festival	3,000		
„ Loss & (embezzlement) by an employee	10,000		

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To Interest	10,000	
,, Legal Expenses	18,000	
,, Investment deposit Account	8,000	
,, Sundry Expenses	16,500	
,, Net Profit	1,52,700	
	3,01,200	3,01,200

Following additional informations are also available:

1. Salary includes a payment of Rs. 8,000 given to an employee outside India and no tax has been deducted at source.
2. W.D.V. of P and M on 1.4.1996 Rs. 80,000. A new Plant & Machinery costing Rs. 40,000 has been installed during the month of November 1996. New P & M is eligible for Depreciation @ 25%.
3. Festival expenses include a gift of Rs. 2,000 given to a relative on her marriage.
4. Sundry expenses include Rs. 5,000 on the maintenance of a guest-house.
5. Travelling expenses include Rs. 4,000 as Hotel Bill of an employee who visited Bombay in connection with business work. His stay in the hotel was for 8 days and his salary was Rs. 2,500 p.m.
6. Legal expenses include a payment of Rs. 12,000 given to a tax consultant in connection with an Income-tax Appeal.
7. A Furniture item of W.D.V. of Rs. 900 has been sold for Rs. 600, and
8. Sundry receipts Rs. 10,000 withdrawn from his public provident fund.

Calculate Business income of Mr. A.

[Hints: Business Income Rs. 1,65,700; Hotel Exp. allowed. Festival Exp. allowed, loss on sale of Furniture item is S.T.C. Loss, withdrawal from PPF is exempted] [P-19].

Q. No. 30

Dr. Satish is a Medical Practitioner. He gives you the following summary of cash book for the year ending 31.3.1997:

	Rs.		Rs.
To Balance	10,000	By Rent of clinic	18,000
,, Consultation fee	60,000	,, Purchase of medicine	38,000
,, Visiting fee	45,000	,, Staff salaries	24,000
,, Gifts and presents	8,000	,, Surgical equipment	40,000
,, Sale of medicine	42,000	,, Motor car expenses	8,000
,, Dividend from U.T.I.	6,000	,, Purchase of motor car	1,40,000
,, Life Insurance Maturity	1,00,000	,, Household expenses	7,000
,, Dividend from N.D.S.	6,000	,, Closing balance	2,000
	2,77,000		2,77,000

Other informations:

(i) 50% of the motor car expenses incurred in connection with profession. Car was purchased in December 1996.

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(*ii*) Household expenses include Rs. 6,800 insurance premium.
(*iii*) Gift and presents include Rs. 3,000 from relatives.
(*iv*) Closing stock for medicine Rs. 12,000 and opening stock on 1.4.96 was Rs. 4,000.

Compute his Taxable Professional Income for the Assessment year 1997-98.

[Bangalore University B.Com.]

[**Hints:** Professional Receipts Rs. 1,52,000 less professional expenses Rs. 93,000 after charging depreciation (Rs. 1,40,000 × 20% = Rs. 28,000 allowed 50% as used for less than 180 days i.e. Rs. 14,000 further reduced to 50% for professional use Rs. 7,000) Professional Gain = Rs. 59,000]

Q. No. 31

From the following Profit and Loss Account of Sri Rama, a sole trader, compute his business income for the Assessment Year 1997-98:—

	Rs.		Rs.
To General expenses	18,000	By Gross profit	89,000
,, Staff salaries	7,000	,, Bad debts recovered	1,000
,, Bad debts	3,000	,, Income tax refund	4,500
,, Depreciation	4,000	,, Dividend on shares (gross)	8,000
,, Advertisement	5,000	,, Dividend on units of U.T.I.	5,000
,, Income tax appeal	11,000		
,, Fire insurance premium on stock	2,000		
,, Donation to N.D.F.	7,000		
,, Patents purchased	10,500		
,, Audit fees	1,000		
,, Provision for doubtful debts	3,800		
,, Life insurance premium	5,200		
,, Net profit	30,000		
	1,07,500		1,07,500

Other informations:

(*i*) Patents are purchased in the previous year.
(*ii*) Bad debts recovered is allowed earlier.
(*iii*) Depreciation for the year is Rs. 4,800.

[Bangalore University B.Com.]

[**Hints:** Business Income Rs. 37,450. Patents expenses to be spread over 14 years. Expenses on Income-tax appeal are fully allowed.]

Q. No. 32

Shri Nehru is the proprietor of a business. His Profit and Loss Account for the year ending March 31, 1997 is as follows :

	Rs.		Rs.
To Establishment	4,800	By Gross Profit	50,840
" Rent, Rates & Taxes	2,900	" interest on Government Securities (Net)	
To General Charges	750	(Tax deducted at	
" Household Expenses	1,730	sources Rs. 520)	5,200
" Commission	1,500	By Rent from House	
" discount and allowance	450	Property	5,400

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" provision for bad debts	1,200	
" postage and telegrams	270	
" Law Charges	450	
" Advertising	1,550	
" Gifts and presents	150	
" Fire Insurance Premium (for goods)	360	
" sales tax	1,250	
" Repairs and Renewals (not for business premises)	480	
" Loss on sale of Motor car (used for private purposes)	1,800	
" Life Insurance Premium	1,790	
" Wealth-tax	740	
" Interest on Capital	350	
" Audit Fee	300	
" Interest on Bank Loan	1,380	
" Provision for Depreciation	2,500	
" Provision for Income-tax	3,900	
" Net Profit transferred to Capital Account	30,840	
	61,440	61,440

Following further information is given :

(*a*) Actual Bad Debts written off during the year amount to Rs. 550.

(*b*) Amount of Income-tax actually paid during the year is Rs. 4,200.

(*c*) Depreciation allowable is Rs. 1,700 as per Income-tax Rules.

(*d*) Advertising expenses include Rs. 550 spent on special advertising campaign to open a new shop in the market.

(*e*) Law charges are in connection with trade mark.

(*f*) Shri Nehru carries on his business from rented premises, half of which is used as his residence. Rent, Rates and Taxes include Rs. 2,400 paid as rent of the premises during the year.

Compute business income of Shri Nehru for the assessment year 1997-98. Workings are to form part of your answer. (*C.A. Inter Nov. 1993*)

[**Hints** : Business Profit Rs. 33,830. Law charges on trademarks allowed ; Expenses on advertisement compaign allowed.]

Q. No. 33

Dr. Nagendra is a renowned medical practitioner, who maintains books of account on cash basis, furnishes receipt and payment account for the year 1996-97 :—

Receipts	Rs.	Payments	Rs.
To Balance b/d	14,000	By rent of clinic	
To consultation fees			
1995-96 3,000		1995-96 600	
1996-97 15,000		1996-97 4,800	
1997-98 2,000		1997-98 600	
	20,000		6,000

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		By Electricity and water Bills	2,000
To visiting fees	30,000	By purchase of professional Books	4,000
To loan from bank	25,000	By Household exp.	7,800
To sale of medicines	60,000	By Collection charges on Dividend	100
To gifts & Presents	5,000	By Motor car purchased	30,000
To Remuneration from Journals	6,000	By Surgical equipment purchased	4,800
To Dividends (gross)	10,000	By Income-tax	10,000
To Interest on Post Office Saving Bank A/c	7,000	By salary to staff	15,000
		By Life Insurance Premium	15,000
		By gift to wife	5,000
		By Interest on Loan (for profession)	2,000
		By car expenses	15,000
		By Purchase of Medicine	40,000
		By Balance c/d	20,300
Total	1,77,000	Total	1,77,000

Compute his taxable professional income for the assessment year 1997-98 after considering the followings:—

(*a*) 1/3 of the use of car relates to his personal use.

(*b*) Depreciation on car is to be allowed @ 20%.

(*c*) Gifts include Rs. 3,000 from patients and Rs. 2,000 from relatives.

(*d*) Closing stock of medicine is Rs. 5,500. *[Mysore B.Com. Oct. 1994]*

[**Hints :** Professional Receipts including remuneration from journals Rs. 1,19,000 less professional expenses Rs. 78,700. Professional Gain Rs. 40,300]

Q. No. 34

From the profit and loss account of Mr. Ramanathan for the year ending 31-3-97, compute his business income :

	Rs.		Rs.
General expenses	63,400	Gross profits	2,65,500
Bad debts	22,000	Commission	18,600
Provision for bad debts	21,000	Brokerage	27,000
Insurance (House)	600	Sundry receipts	22,500
Salary to staff	36,000	Bad debts recovered	
Salary to Ramanathan	22,000	(earlier disallowed	
Interest on Bank over draft	62,000	as deduction)	1,000
Interest on loan to Mrs. Ramanathan	4,000	Interest on deposit with a trust	15,000
Interest on capital of Ramanathan	13,000	Interest on units of U.T.I.	13,000
		Rent from house Property	12,000

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Depreciation on building	60,000		
Advertisement expenditure	8,000		
Contribution to employees' RPF	12,000		
Net profit	50,600		
	3,74,600		3,74,600

Other informations:

(*a*) The amount of depreciation allowable on building is 40,200 as per Income tax Rules.

(*b*) Advertisement expenditure includes Rs. 5,000 being cost of permanent sign board fixed on office premises.

(*c*) Income of Rs. 10,000 accrued during the year is not recorded in the Profit and Loss Account.

(*d*) Ramanathan pays Rs. 12,000 as premium on own Life Insurance Policy of Rs. 90,000.

(*e*) General expenses includes Rs. 4,500 given to Mrs. Ramanathan for arranging a party in honour of her friend.

(*f*) Employee's contribution to provident fund for the last two months @ Rs. 1,000 P.M. has not been paid to appropriate authority within due date.

[**Hints** : Cost of permanent sign board allowed ; Provident Fund contribution disallowed upto Rs. 2,000 ; Accrued income is Taxable ; Business Profit Rs. 102,500].

Q. No. 35

Following are the details of income from the bodies of M/s Kartik Traders, owned by Mr. Sharma for the year 1996-97:—

PROFIT AND LOSS ACCOUNT

Dr.	Rs.	Cr.	Rs.
To Opening Stock	72,000	By Sales	12,00,000
" Purchases	8,00,000	" Closing Stock	81,000
" Wages	30,000		
" Carriage & Freight	40,000		
" G.P. c/d	3,39,000		
	12,81,000		12,81,000
To Staff Salaries	90,000	By G.P. b/d	3,39,000
" Rent & Taxes	20,000	" Life Policy amount	5,000
" Advertisement	20,000	" Sale of old machinery	2,000
" Audit fee	20,000	" Interest & dividends	4,000
" Donations	10,000		
" Income Tax	10,000		
" Reserve for Bad debts	10,000		
" Depreciation Reserve	10,000		
" Sales Tax	10,000		

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" Printing & Stationery	20,000		
" Contribution to staff welfare Fund	10,000		
" Patents purchased	90,000		
" Int. on capital	10,000		
" N.P. c/d	20,000		
	3,50,000		3,50,000

Additional informations:

1. The Opening stock has been vlaued at cost minus 10% basis, but not the closing stock.
2. Purchase include a payment of Rs. 20,000 by a bearer cheque to a supplier.
3. Depreciation allowable as per I.T. rules for the year was Rs. 8,000.
4. Freight includes Railway Demurrage Rs. 2,000 and railway penalty Rs. 5,000.
5. Advertisement includes expenses on 30 gift articles given to select customers at a cost of Rs. 300 each.
6. Patents purchased have been used in the business for the past 5 years under an agreement.
7. Entertainment expenses of Rs. 8,000 has been spent in the p.y. 96-97 [Not debited].
8. He has carried forward the Business loss of Rs. 6,000, from the earlier Assessments.

Compute his net business income for the assessment year 1997-98

[Bangalore B. Com. Nov. 1993]

[**Hints :** Business income Rs. 1,34,000; Demurrage allowed. Payment in cash 20% disallowed; patent right to be disallowed Rs. 80,000 (8/9) B/F Business loss to be adjusted (Rs. 1,34,000 – 6,000)]

Q. No. 36

From the particulars given below compute the business income for the assessment year 1997-98 :

PROFIT AND LOSS ACCOUNT

	Rs.		Rs.
To salary to staff	2,65,000	By Gross Profit	6,50,800
" Bad debts	8,000		
" Bonus	24,000	By rent of quarters	
" Reserve for bad &		given to employee	24,000
doubtful debts	12,000		
To Provision for income tax	10,000	By Customs duty recovered	
		from Govt. (no allowed	
" Expenditure on acquisi-		earlier)	30,000
tion of copy right	8,400	By bad debts	
		recovered	
" Cost of Extention of	16,000	(Out of which 3,000	
office building		were not allowed	6,000
" Legal expenses	24,000	earlier)	
" Expenses on diwali	10,000		

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" General Expenses	6,600	By sundry receipts	8,000
" Provision for Sales tax	12,800		
" Provision for excise duty	40,500		
" Lumpsum amount paid to acquire technical know-how	24,000		
" Lumpsum amount paid to acquire a patent right	28,000		
" Legal expenses regarding income tax appeal	22,000		
" Net Profit	2,07,500		
	7,18,800		7,18,800

Other relevant information are :

1. General expenses include expenditure of Rs. 3,000, incurred on the training of an employee.
2. Actual sales tax is deposited as under :
   —Rs. 6,800 on 20.6.97
   —Rs. 6,000 on 20.11.97
3. Actual excise duty is deposited as under :
   —Rs. 20,000 on 20.6.97
   —Rs. 20,500 on 20.10.97
   —Date of filing of return is 31.10.97
4. Salary of staff includes a payment of Rs. 60,000 paid to a relative employee which is considered to be unreasonable upto Rs. 20,000.
5. Provisions for income-tax is excessive to the tune of Rs. 4,000
6. Payment of bonus of Rs. 10,000 payable during previous year 1994-95, Rs. 6,000 for the previous year 1995-96 and remaining Rs. 8,000 for the previous year 1996-97.
7. Income-tax appeal expenses are paid as follows :
   (*i*) Rs. 6,000 paid to an employee for preparing an income-tax appeal related to previous year 1995-96.
   (*ii*) Rs. 4,000 loan advocate to obtain an advice on income-tax matters.
   (*iii*) Rs. 12,000 to a Chartered Accountant, who is not an employee, to get advice regarding income-tax matters.
8. The particulars about the assets of the business are as under :
   (*i*) Building (Office) W.D.V. on 1.4.96 Rs. 4,20,000
   (*ii*) Godown W.D.V. on 1.4.96 Rs. 2,00,000
   (*iii*) Plant & Machinery W.D.V. on 1.4.96 Rs. 2,40,000
9. Technical know how was acquired from an institution, which was wholly financed by Govt. of India.

[Hints : Income-tax appeal expenses, and bonus fully allowed ; sales tax allowed Rs. 6,800, excise duty fully allowed ; Cost of copyright and patent right allowed upto $^1/_{14}$th of Rs. 36,400 ; Depreciation allowed Rs. 1,23,600; Business Profit Rs. 1,64,700.]

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Q. No. 37

A has debited the following amounts of expenditure in his profit and loss account for the year ending 31st March, 1997.

	First Payment		*Second Payment*	
Payments out-standing as on 31.3.1997	Date of Payment	Amount Paid (Rs.)	Date of Payment	Amount Paid (Rs.)
(1)	(2)	(3)	(4)	(5)
Excise duty payable: Rs. 32,000	20.6.97	12,000	23.1.98	20,000
Sales tax payable: Rs. 48,000	15.10.97	48,000	—	—
Bonus payable to employees: Rs. 67,000	12.5.97	50,000	15.12.97	17,000
Interest payable to PFC on loan Rs. 50,000	23.5.97	30,000	16.1.99	20,000
Interest payable to Syndicate Bank on loan; Rs. 43,000	26.4.98	43,000	—	—
Income tax payable: Rs. 1,21,000	30.5.97	1,21,000	—	—
Commission payable to employees: Rs. 1,60,000	31.10.97	1,00,000	31.10.98	60,000

Due date of filing return of income is 31st August, 1997. Find out the previous years in which the aforesaid payments are deductible. A maintains books of account on the basis of mercantile system of accounting

[Company Secretary Inter June 1991]

[**Hints** : Excise duty Rs. 12,000 to be debited in previous year 96-97 and Rs. 20,000 in 1997-98; Sales tax to be allowed in previous year 1997-98; Bonus Rs. 50,000 in 96-97 and Rs. 17,000 in 97-98; Interest on loan to PFC Rs. 30,000 in 96-97 and Rs. 20,000 in 98-99; Interest on Bank Loan Rs. 43,000 in 98-99; Income-tax not allowed; Commission to employees to be allowed Rs. 100,000 in 1997-98 and Rs. 60,000 in 1998-99]

QUESTIONS

1. What do you understand by the term 'business' and 'profession' as used u/s 28 of the Income-tax Act ?
2. What are the charging provisions u/s 28 under the head "Profits and Gains of Business or Profession' ?
3. Explain in brief the provisions relating to claim of expenses on scientific research ? *[Company Secretary Inter Dec. 1992]*
4. What are the provisions of law relating to preliminary expenses ?
5. Explain the concept of deemed profits u/s 41 ?

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4 PROFITS AND GAINS-II—DEPRECIATION

What is depreciation—Conditions for charge of depreciation—assets—used for business—New method of charging depreciation—Block of assets—rates of depreciation—Actual cost of assets—Written down value of assets—Types of depreciation—Computation of depreciation—Misc. provisions about depreciation—Investment allowance, Investment Deposit Account—Development Allowance, and Tea Development Account—Reserve for shipping business—Illustrations—Questions.

I. DEPRECIATION [Section 32]

Depreciation is a very important item treated under the head Profit & Gains of Business or Profession. In simple language depreciation is decrease in the value of an asset due to its wear and tear and passage of time. The Income-tax Act 1961 nowhere defines the term depreciation. Depreciation is the process of allocating the cost of long-term asset to the time periods in which it is used in a systematic and rational manner. As time passes the value of a capital asset goes on decreasing and depreciation measures this decrease in monetary value which in turn is treated as business expenditure and debited to profit and loss account of the assessee.

Why depreciation. Depreciation is calculated with following three objects:

(*a*) To arrive at the real business profits by charging the monetary value of decrease in efficiency of any asset used for the business.

(*b*) To determine the book value of asset at any given time so as to assess the net worth of the business.

(*c*) To know the real position about the asset and to arrange for its replacement or renewal by setting aside a specified sum out of each year's profits.

Charge of Depreciation

Depreciation can be charged out of

(*a*) *Profits & Gains of Business or profession* carried on by the assessee during relevant previous year; or

(*b*) *Income from other sources* in case of assets let out for a certain period of time and letting is not the regular business of assessee [Section 56(2)(*ii*) and (*iii*)].

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CONDITIONS FOR DEPRECIATION

In order to claim depreciation, certain conditions have to be fulfilled. These conditions are either laid down in law or Income-tax Rules 1962 or as per case decisions. These conditions are:

1. Depreciation is allowed only on capital assets. Depreciation is allowed only on the capital assets namely buildings, machinery, plant and furniture. Capital assets other than these shall not be eligible for depreciation. As such no depreciation is allowed on goodwill, patent rights or animals etc. All these four groups of assets are explained below:

(*a*) *Building.* Any structure having walls and a room may be made of bricks or wood but which can be put to use is called building. It includes factory, office, godown, workshop, residential house of employees, school, hospital, creche, club, canteen etc. constructed for welfare of employees.

The cost of building does not include cost of land or site. It has been held that depreciation is admissible only on building and not on cost of land. (*C.I.T. vs. Alps Theatre 1967*).

Depreciation can be claimed on building constructed on a piece of land taken on lease or rent.

The term 'building' includes in itself the roads, bridges, wells and tubewells etc.

Classification of buildings. With effect from assessment year 1988-89 the new rate schedule (given later) has classified the buildings into four categories:

(*i*) *Buildings (Non-factory)*—Includes buildings used for residential purposes; but does not include such buildings which are used as Hotels and residential houses for employees if the plinth area of such house does not exceed 80 square metres of each unit.

(*ii*) *Buildings (factory)*—Non-residential buildings are included in this category but does not include Hotel building and such residential houses whose plinth area does not exceed 80 square metres.

(*iii*) *Buildings (Priority)*—The hotel buildings and residential houses for employees provided the plinth area of such houses does not exceed 80 sq. metres, are covered in this category.

(*iv*) *Buildings (Temporary Structures)*—Includes purely temporary creation such as wooden structures.

(*b*) *Machinery.* Next asset to be covered under the definition of capital assets is machinery. Machinery is that complex combination of mechanical parts which help in production. It is a complex system of appliances used to achieve a desired result.

(*c*) *Plant.* U/s 40(3) of the Income-tax Act 1961 the word plant includes ships, vehicles, scientific apparatus, technical know-how reports, surgical equipment, office equipment etc., used for the purposes of business or profession of the assessee. Sanitary and pipeline fittings of a hotel, service lines and switch gears of electric supply company are also included in the definition of *Plant*. The warehouses, roads

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constructed within the factory premises, water storage tanks used for irrigation of agricultural lands are not included in the definition of *'Plant'*.

(*d*) *Furniture.* The term furniture includes all articles of convenience or decoration used with the object of furnishing or decorating some premises. The decoration articles are also included in the definition of furniture.

2. Use of asset during the year. Till assessment year 1991-92 depreciation for full year was allowed even if asset was used for one day during the relevant previous year. But the Finance (No. 2) Act 1992 has inserted a proviso by which the depreciation has been restricted. With effect from 1.4.92 *i.e.* assessment year 1992-93 the depreciation is to be calculated as under:

(*a*) In case any asset falling within a block is used for a period of less than 180 days in relevant previous year for the business or profession—depreciation shall be allowed at the rate of 50% of amount calculated at prescribed rate;

(*b*) In case asset is used for 180 days or more—full depreciation shall be allowed.

3. Block of assets. With the introduction of new method of charging depreciation, the term **block of assets** has been inserted in the Income-tax Act 1961. Under section 2(11) it means a group of assets falling within a class of assets being buildings, machinery, plant and furniture in respect of which the same percentage of depreciation is prescribed. This concept has come into effect from 2.4.1987 *i.e.* assessment year 1988-89.

4. Asset must be owned by the assessee. To claim depreciation it is essential that the assessee must be owner of the business. Owner is that person who can exercise the rights of owner on his own behalf and he is entitled to income from such asset. Assessee cannot claim any depreciation unless he is the owner although he might be using it. In case of hire-purchase agreements it is essential to find out the time at which ownership is transferred to buyer from seller. In case the agreement provides for the transfer of ownership at the time of agreement itself, the assessee can debit full depreciation on such assets but cannot debit hire charges to his P & L A/c. In case the ownership in property has not passed to the buyer, the buyer cannot charge depreciation. It can debit hire charges to its P & L A/c.

5. Assets actually used for the business in the previous year. The deduction of depreciation allowed only on those assets which are actually used in the business or profession of the assessee in the previous year. But in case any plant, machinery etc. is kept as standby to be used in case of emergency or break down, depreciation on such assets is also allowed.

If any portion of the assets is not used for the purposes of the business or profession of the assessee, depreciation will not be allowed on such part of the asset. For example, car is partly (say 50%) used for business and partly for the private use of the partners. In this case, only half of the normal depreciation can be charged from the profit and loss account of the business.

In case any plant, machinery and furniture is let on hire, the depreciation is allowed on such assets. Similarly, if any building is given on hire along with

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machinery, plant, furniture, etc. and letting of building is inseparable from letting of the machinery, plant and furniture, the allowance of depreciation is allowable.

Whether a unit has commenced commercial production or not is not a precondition for allowing depreciation u/s 32 or Investment Allowance u/s 32A *[C.I.T. v. Industrial Solvents & Chemical (P) Ltd. (Bombay)]*.

6. No depreciation in the year of sale of asset. Depreciation is only a book entry which is passed on the last day of the year. If any assets are sold during the year, such assets will not be with the business, so depreciation cannot be charged on the assets which are not in existence at that time. The deduction of depreciation will not be allowed on assets which are sold during the year. The loss suffered due to the sale of the asset, however, will be considered under Short Term Capital Gain.

The provisions relating to Terminal depreciation and Balancing charge have lost their value with the introduction of new scheme of depreciation. Hence the Taxation Laws (Amendment) Act has omitted the sections 32(1)(iii) and 41(2). Under the new system the money payable in respect of asset sold, discarded, demolished, or destroyed will be reduced from the written down value of such block.

7. Full particulars of the asset, on which depreciation is to be charged, must be furnished to the A.O. All the assessees who are to charge depreciation, must furnish all the particulars of the asset to the concerned Assessing Officer. The assessee has to fill in a form which is prescribed for this purpose.

8. Depreciation is allowed on the basis of written down value of the asset. In case of all assets, it is to be calculated on the basis of the written down value of the assets. When a new asset is purchased, the cost price of same will be the written-down value of the asset in the first year.

9. Meaning of word Plant. Plant includes ships, vehicles, books, scientific apparatus and surgical equipment used for the purpose of the business or profession on but does not include tea, bushes and livestock.

10. Car manufactured outside India and imported into India after 28.2.1975. No depreciation shall be allowed on motor cars manufactured outside India and acquired by an Indian assessee after 28.2.1975. However, depreciation at prescribed rates shall continue to be allowed, if such car is to be used for hire to tourists *i.e.* for tourist taxi purposes.

The Finance (No. 2) Act has changed the language of this proviso as under:

No depreciation shall be allowed in respect of

(*a*) any motor car manufactured outside India where such motor car is acquired by the assessee after 28th day of February 1975 unless it is used—

(*i*) in a business of running it on hire for tourist; or

(*ii*) outside India in his business or profession in another country; and

(*b*) any machinery or plant if the actual cost thereof is allowed as a deduction in one or more years under an agreement entered into by the Central Govt. under section 42. *[Proviso to section 32(1)]*.

11. Depreciation on Motor Taxies, Lorries, Trucks etc. used for hiring. The higher rate of depreciation is allowed (40%) on motor taxies, lorries and trucks if these are hired out to outside persons.

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Vide circular No. 652 dt. 14.6.93 this higher rate will be applicable on motor lorries used in the assessee's business of transportation of goods on hire. This higher rate will not apply if the motor lorries, buses etc. are used in some other non-hiring business of the assessee.

12. Depreciation on assets used in Guest houses. [Section 37(4)]. Depreciation on any asset which is used in Guest Houses maintained by the assessees, cannot be debited to Profit and Loss Account of the assessee.

13. In case of succession or amalgamation. Depreciation will be calculated on plant and machinery, building or furniture for full year and shall be allocated on the basis of number of days for which assets were used by predecessor and successor or by amalgamating company and amalgamated company as the case may be.

NEW METHOD OF DEPRECIATION

With effect from 2.4.1987, the method of charging of depreciation has been completely changed. The various types of assets have been regrouped into blocks of assets on the basis of rate of depreciation. Higher rates of depreciation have been prescribed and some types of depreciation have been eliminated. The new scheme of depreciation is discussed as under.

1. Block of assets [Section 2(11)]

The basis of charge of depreciation has been shifted from individual assets to group of assets. The assets have been divided into blocks on the basis of rates of depreciation prescribed under rule 5 of the Income-tax Rule 1962. This concept has become effective from 2.4.1987 *i.e.* in relation to assessment year 1988-89.

2. New rates of Depreciation

SCHEDULE OF RATES

Sl. No.	*Assets*	*Block of assets*	*Rate of depreciation*
1	*2*	*3*	*4*
I.	Buildings	1. Buildings which are used mainly for residential purposes other than those given at (2) and (3) below.	5%
		2. Buildings which are not used mainly for residential purposes and which are not covered at (3) below.	10%
		3. (*i*) Buildings used as hotels.	
		(*ii*) Buildings with dwelling units each with plinth area not exceeding 80 square metres.	20%
		4. Purely temporary erection such as wooden structures	100%
II.	Furniture and Fittings	1. Furniture and fitting—Not fittings in sub-item (2) below.	10%
		2. Furniture and fittings used in hostels, restaurants and boarding houses; schools,	

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		colleges and other educational institutions; libraries, welfare centres; meeting halls; cinema houses; theaters and circuses; and furniture and fittings let out on hire for use on the occasion of marriages and similar functions.	15%
III.	Machinery and plant	1. Machinery and plant, scooters & cars (cars acquired before 1.4.90) other than those covered by (3) and (4) below.	25%
		2. Cars acquired on or after 1.4.90.	20%
		3. (*i*) Aeroplanes—Aero engines (*ii*) Motor buses, motor lorries and motor taxis used in a business of running them on hire (*iii*) Moulds used in rubber and plastic goods factories	40%
		(*iv*) Air pollution control equipments, being— (*a*) Electrostatic precipitation systems (*b*) Felt-filter systems (*c*) Dust collector systems (*d*) Scrubber-counter current/venturi/ packed-bed/cyclonic scrubbers (*e*) Ash handling system and evacuation system	40%
		(*v*) Water pollution control equipments, being— (*a*) Mechanical screen system (*b*) Aerated detritus chambers (including air compressor) (*c*) Mechanically skimmed oil and grease removal systems (*d*) Chemical feed systems and flash mixing equipment (*e*) Mechanically flocculators and mechanically reactors (*f*) Diffused air/mechanically aerated activated sludge systems (*g*) Aerated lagoon systems (*h*) Biofilters (*i*) Methane-recovery anaerobic digester systems (*j*) Air floatation systems (*k*) Air/steam stripping systems (*l*) Urea hydrolysis systems (*m*) Marine outfall systems (*n*) Centrifuge for dewatering sludge (*o*) Rotating biological contractor or bio-disc (*p*) Ion exchange resin column (*q*) Activated carbon column	40%

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1	2	3	4
		(*vi*) Solidwaste control equipments, being caustic/lime/chrome/mineral/cryolite recovery system	40%
		(*vii*) Machinery and plant used in semi-conductor industry covering all integrated circuits (ICs) (excluding hybrid integrated circuits) ranging from small scale integration (SSI) to large scale integration/very large scale integration (LSI/VLSI) as also discrete semi-conductor devices such as diodes, transistors, thristors, triacs etc.) other than those covered by entries (*iv*), (*v*) and (*vi*) of this sub-item and sub-item (3) below	40%
	3.	(*i*) Wooden parts used in artificial silk manufacturing machinery	100%
		(*ii*) Cinematograph films—bulbs of studio lights	100%
		(*iii*) Energy saving devices, being—	
		A. Specialised boilers and furnaces—	
		(*a*) Ignifluid/fluidized bed boilers	
		(*b*) Flameless furnaces and continuous pusher type furnaces	
		(*c*) Fluidized bed type heat treatment furnaces	100%
		(*d*) High efficiency boilers (thermal efficiency higher than 75 per cent in case of coal fired and 80 per cent in case of oil/gas fired boilers).	
		B. Instrumentation and monitoring system for monitoring energy flows:	
		(*a*) Automatic electrical load monitoring systems	
		(*b*) Digital heat loss metres	
		(*c*) Micro-processor-based control systems	
		(*d*) Infra-red thermography	100%
		(*e*) Meters for measuring heat losses, furnace oil flow, steam flow, electric energy and power factor meters	
		(*f*) Maximum demand indicator and clamp on power metres	

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(*g*) Exhaust gases analyser	
(*h*) Fuel oil pump test bench	
C. Waste heat recovery equipments:	
(*a*) Economisers and feed water heaters	
(*b*) Recuperators and air pre-heaters	100%
(*c*) Heat pumps	
(*d*) Thermal energy wheel for high and low temperature waste heat recovery	
D. Co-generation systems:	
(*a*) Back pressure pass out, controlled extraction-*cum*-condensing turbines for cogeneration along with pressure boilers	
(*b*) Vapour absorption refrigeration systems	100%
(*c*) Organic ranking cycle power systems	
(*d*) Low inlet pressure small steam turbines	
E. Electrical equipments:	
(*a*) Shunt capacitors and synchronous condenser systems	
(*b*) Automatic power cut off devices (relays) mounted on individual motors	100%
(*c*) Automatic voltage controller	
(*d*) Power factor controller for AC motors	
(*e*) Solid state devices for controlling motor speeds	
(*f*) Stenters	
F. Burners:	
(*a*) 0 to 10 per cent excess air burners	100%
(*b*) Emulsion burners	
(*c*) Burners using air with high preheat temperature (above 300°C)	
G. Other equipments:	
(*a*) Wet air oxidation equipment for recovery of chemicals and heat	
(*b*) Mechanical vapour recompressors	
(*c*) Thin film evaporators	100%
(*d*) Automatic micro-processor based load demand controllers	
(*e*) Coal-based producer gas plants	
(*f*) Fluid drives and fluid couplings	
(*g*) Turbo charges/super charges	

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1	2	3	4
		(*iv*) Floor mills—Rollers	100%
		(*v*) Gas cylinders including valves and regulators	100%
		(*vi*) Glass manufacturing concerns—Direct fire glass melting furnaces	100%
		(*vii*) Iron and steel industry—Rolling mill rolls	100%
		(*viii*) Match factories—Wooden match frames	100%
		(*ix*) Mineral oil concerns—	100%
		(*a*) Plant used in field operations (above ground) distribution—Returnable packages	
		(*b*) Plant used in field operations (below ground), but not including kerbside pumps including underground tanks and fittings used in field operations (distribution) by mineral oil concerns	
		(*x*) Mines and quarries—	100%
		(*a*) Tubs, winding ropes, haulage ropes and sand stowing pipes	
		(*b*) Safety lamps	
		(*xi*) Salt works—Salt pans, reservoirs and condensers, etc., made of earthy, sandy or clayey material or any other similar material	100%
		(*xii*) Sugar works—Rollers	100%
		(*xiii*) Renewal energy devices being—	
		(*a*) Flat plate solar collectors	
		(*b*) Concentrating and pipe type solar collectors	
		(*c*) Solar cookers	
		(*d*) Solar water heaters and systems	
		(*e*) Air/gas/fluid heating systems	100%
		(*f*) Solar crop driers and systems	
		(*g*) Solar refrigeration, cold storages and air-conditioning systems	
		(*h*) Solar steels and desalination	
		(*i*) Solar power generating systems	
		(*j*) Solar pumps based on solar thermal and solar photovoltaic conversion	
		(*k*) Solar photovoltaic modules and panels for water pumping and other applications	
		(*l*) Wind mills and any specially designed devices which run on wind mills	

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		(*m*) Any special devices including electric generators and pumps running on wind energy	100%
		(*n*) Biogas plant and biogas engines	
		(*o*) Electrically operated vehicles including battery powered or fuel-cell powered vehicles	
		(*p*) Agricultural and municipal waste conversion devices production energy	
		(*q*) Equipment for utilising ocean waves and thermal energy	
		(*r*) Machinery and plant used in the manufacture of any of the above sub-items.	
		4. Books required for professional use	**100%**
IV.	Ships	1. Ocean-going ships including dredgers, tugs, barges, survey launches and other similar ships used mainly for dredging purposes and fishing vessels with wooden hull	20%
		2. Vessels ordinarily operating on inland waters not covered under (3) below	10%
		3. Vessels ordinarily operating on inland waters other than speed boats	20%

3. Actual cost of assets [Section 43 (1)]

In case of a new asset, its *'actual cost'* is to be added in the value of block of assets. In case of a new unit, depreciation is to be based on *'actual cost'*. These two reasons make it compulsory for us to study the concept of actual cost.

(*i*) *Actual cost means cost of asset actually met by assessee*

U/s 43 (1) actual cost means the actual cost of the assets to the assessee reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority.

In case any subsidy or grant is received by the assessee as an incentive for some purpose, the amount so received cannot be called as part of the actual cost even if it is appropriated by the assessee against such asset. In such case the amount of subsidy received shall not be reduced out of actual cost for calculating depreciation. *[C.I.T. vs. P.J. Chemicals Ltd. (S.C.) 1994 (122 Taxation 682)].*

In case there is direct nexus between subsidy and cost of asset, such subsidy shall be reduced out of actual cost.

In case any part of the cost is met by consumers (*e.g.* cost of service lines of an electricity supply company met partly by company and partly by consumer) the actual cost shall be the cost of asset less amount paid by consumers.

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(*ii*) *Actual cost to include certain expenses*

Actual cost of asset shall include the following:

(*a*) Cost paid for acquiring the asset;

(*b*) Cost of installation;

(*c*) Expenses on insurance, freight, loading and unloading;

(*d*) Expenses on modifications and repairs incurred before the actual use of asset;

(*e*) Expenses on salaries, rent, lighting etc. relating to the period before production has commenced can be added in actual cost;

(*f*) Interest paid in connection with purchase of asset and bank charges.

But with the introduction of explanation of Finance Act 1986 and that too with retrospective effect *i.e.* 1.4.74, any amount of interest paid or payable in connection with the acquisition of asset the amount of interest relating to any period after such asset has been put into use shall not be included in actual cost and shall be deemed never to have been included. It implies that interest in connection with the acquisition of asset relating to the period prior to the date on which asset is put into use can be capitalised and shall be included in the actual cost.

(iii) Motor car imported into India after 28.2.1975 [Section 32 (1) (*ii*)]

No depreciation is allowed on any motor car manufactured outside India and used for assessee's business unless it is used in business of running it on hire for tourists.

During the period 1.4.67 to 28.2.1975 depreciation was allowed on imported cars but in case actual cost exceed Rs. 25,000, excess was ignored and depreciation was calculated on Rs. 25,000 as actual cost. After 28.2.1975 no depreciation is allowed on imported cars and restriction of price has been removed. [43 (*i*) Proviso].

(*iv*) *Asset earlier used for scientific research.* When an asset is used in business after it ceases to be used for scientific research related to that business, the actual cost of the asset shall be the actual cost to the assessee as reduced by the amount of any deduction allowed in respect of it. [Section 43 (*i*) Explanation (1)].

(*v*) *Asset acquired by way of gift or inheritance.* Where an asset is acquired by the assessee by way of gift or inheritance, the actual cost of the asset to the assessee shall be

(*a*) actual cost as reduced by any depreciation claimed upto 31.3.88; and

(*b*) any depreciation claimed on such asset after 31.3.88 as if it was only one asset of the block. [*Section 43(1) Explanation (2)*]

(*vi*) *Transfer of asset to reduce tax liability.* Where the assets were at any time used by the other person for the purpose of his business or profession and the Assessing Officer is satisfied that the main purpose of the transfer of such assets was the reduction of a liability of income-tax (by claiming depreciation with reference to enhanced cost), the actual cost of the assessee shall be such an amount as the Assessing Officer may, with the previous approval of the Assistant Commissioner, determine having regard to all the circumstances of the case. [Section 43 (*i*) Explanation (3)].

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(*vii*) *Asset re-acquired.* Where assets which had once belonged to the assessee and had been used by him for the purpose of his business or profession and thereafter ceased to be his property by reason of transfer or otherwise are re-aquired by him, the actual cost to the assessee shall be

(*a*) actual cost as reduced by any depreciation claimed upto 31-3-88; and

(*b*) any depreciation claimed on such asset after 31-3-88 as if it was only one asset of the block.

OR

the actual price at which asset is reacquired which ever is less.

(*viii*) *Building brought into use after 28-2-1946.* Where a building previously the property of the assessee is brought into use for the purpose of the business or profession after 28th February 1946, the actual cost of the assessee shall be the actual cost of the building to the assessee as reduced by an amount equal to the depreciation calculated at the rate in force on the date that would have been allowable had the building been used for the aforesaid purpose since the date of its acquisition by the assessee. [Section 43 (*i*) Explanation (5)].

(*ix*) *Asset transferred by a holding company to its subsidiary company.* When any capital asset is transferred by a holding company to its subsidiary company or by a subsidiary company to its holding company, then if the subsidiary company is an Indian company and is a 100% owned company the actual cost of the transferred capital asset to the transferee company shall be taken to be the same as it would have been if the transferred company had continued to hold the capital asset for the purpose of its business. [Section 43 (*i*) Explanation (6)].

(*x*) *In a scheme of amalgamation.* Where in a scheme of amalgamation, any capital asset is transferred by the amalgamating company to the amalgamated company and the amalgamating company is Indian company, the actual cost of the transferred capital assets to the amalgamated company shall be taken to be the same as it would have been if the amalgamating company had continued to hold the capital asset for its own business [Section 43 (1) Explanation (7)].

(*xi*) *On partition of HUF.* In case an assessee has acquired an asset on partition of HUF; the cost of such asset to the assessee will be the cost at the time of partition and not the cost at which it was acquired by HUF.

4. Method of Depreciation

Depreciation on all assets is to be calculated on diminishing value basis *i.e.* written down value method. Previously in case of ocean-going ships, depreciation was allowed on actual cost basis but under the new method only W.D.V. method has to be applied.

5. Written down value

U/s 43 (6) written down value (W.D.V.) means:

(*a*) In the case of asset acquired in the relevant previous year, the actual cost to the assessee shall be deemed as W.D.V.

(*b*) In case of assets acquired before the previous year, the W.D.V. is the actual cost less total amount of depreciation (*i.e.* Normal depreciation +

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Extra Normal depreciation + Extra shift allowance + initial depreciation claimed after 31-3-83). Any allowance in respect of any depreciation carried forward shall be deemed to be depreciation actually allowed. But initial depreciation allowed after 31-3-83 only is to be deducted while calculating W.D.V.

(*c*) *W.D.V. for the assessment year 1988-89.*

The written down value for the purposes of calculating depreciation for the assessment year 1988-89, shall be calculated as under:

(*a*) **Take** the aggregate of the written down value of all the assets falling within that block of assets at the beginning of previous year;

(*b*) **Add** the actual cost of any asset acquired during the previous year and falling in same block of assets;

(*c*) **Deduct** the moneys receivable by assessee together with the scrap value in regard to any asset of same block which is sold, discarded, demolished or destroyed during the previous year.

The resultant amount shall be the written down value for calculating depreciation [Section 43 (6) (*c*)].

W.D.V. for the assessment year 1989-90 and onwards

The written down value for the purposes of calculating depreciation for the assessment year 1989-90 shall be computed as under:

(*a*) The written down value calculated above shall be reduced by the amount of depreciation actually allowed in respect of the block of assets for the respective previous year. The balance shall become the opening W.D.V. for the next previous year;

(*b*) Add the actual cost of any asset acquired during the previous year and falling in same block of assets;

(*c*) Deduct the moneys receivable by assessee together with the scrap value in regard to any asset of same block which is sold, demolished, destroyed or discarded in the relevant previous year.

The resultant amount shall be the W.D.V. for the calculation of further depreciation.

Illustration 1. W.D.V. of block of P & M on 1.4.96 was Rs. 5,95,000. During the year 1996-97 a new item costing Rs. 1,50,000 was acquired in May, 1996 and an item was sold on 15.9.96 for Rs. 79,000. Calculate the W.D.V. of this block of assets and calculate the depreciation @ 25% in relation to assessment year 1997-98.

Solution. ***Assessment year 1997-98***

	Rs.
Written down value of Blocks of Assets	5,95,000
Less: Money realised on account of asset sold during the year	79,000
	5,16,000

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Add: Cost of new asset acquired and put into use during the year [May, 1996]	1,50,000
W.D.V. on 31.3.97	6,66,000
Depreciation for this block of assets @ 25%	1,66,500
W.D.V. on 1.4.97	4,99,500

6. Computation of Depreciation

Once written down value of each block has been calculated, the calculation of depreciation becomes very easy.

$$\text{Depreciation} = \text{W.D.V. of Block} \times \frac{\text{rate of depreciation for that block}}{100}$$

In case assessee has only one asset in a block of assets, such asset alone will get the treatment of block of asset.

In case of a new business actual cost of assets in a particular block shall be deemed as W.D.V. for the first year.

Illustration 2. Calculate depreciation which can be debited to P. & L. A/c for the year ending on 31.3.97.

Sr. No.	*Particulars*	*W.D.V. on 1.4.96*	*Additions during the year*	*Money realised on Assets destroyed*	*Rate of Dep.*
1.	Factory Building	3,50,000	1,00,000	60,000	10%
2.	Residential Houses for employees—plinth area of each unit not exceeding 80 sq. metres	10,00,000	2,00,000	—	20%
3.	Furniture & Fittings	15,000	5,000	—	10%
4.	(*a*) Plant & Machinery	20,40,000	6,50,000	2,70,000	25%
	(*b*) Air compressor	20,000	—	—	40%
	(*c*) Solar power generator		1,50,000	—	100%
5.	Cost of 2 calculators purchased @ Rs. 4,000 per calculator	8,000	—	—	—

Note: Plant and Machinery was acquired and put into use in Nov. 1996. But solar generator was put to use in June, 1996. Calculators were acquired on 14.6.96.

Solution

Sr. No.	*Particulars*	*W.D.V. on 1.4.96. Rs.*	*Depreciation Rs.*
1.	*Building* 10% Block		
	W.D.V. on 1.4.96	3,50,000	
	Add : Actual cost of new asset	1,00,000	
		4,50,000	
	Less : Money realised	60,000	
	W.D.V. on 31.3.97	3,90,000	
	Dep. @ 10%		39,000

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2.	*Buildings* –20% Block		
	W.D.V. on 1.4.96	10,00,000	
	Add: Actual cost of new asset	2,00,000	
		12,00,000	
	Dep. @ 20%		2,40,000
3.	*Furniture* 10% Block		
	W.D.V. on 1.4.96	15,000	
	Additions during the year	5,000	
		20,000	
	Depreciation @ 10%		2,000
4.	*Plant and Machinery*—25% block		
	W.D.V. on 1.4.96	20,40,000	
	Add: Cost of P & M acquired—used for less than 180 days	6,50,000	
	Calculators acquired on 14.6.96	8,000	
		26,98,000	
	Less: Money realised	2,70,000	
	W.D.V. on 31.3.97	24,28,000	
	Depreciation		
	On new asset used for less than 180 days (6,50,000 × 25% × 1/2)		81,250
	On balance W.D.V. [(24,28,000 – 6,50,000) × 25%]		4,44,500
5.	*Plant and Machinery*—40% Block		
	W.D.V. on 1.4.96	20,000	
	Depreciation @ 40%		8,000
6.	*Plant and Machinery*—100% Block		
	Cost of solar generator	1,50,000	
	Depreciation @ 100%		1,50,000
	Total Depreciation		9,64,750

Illustration 3. M/s A & Bros. have following assets on 1.4.96 :

Sr. No.	*Assets*	*W.D.V. on 1.4.96*	*Additions during the year*	*Scrap value of asset put out of use during the year*	*Rate of depreciation*
		Rs.	*Rs.*	*Rs.*	
1.	Plant & Machinery	42,20,000	6,90,000	2,10,000	25%
2.	Aircraft	34,50,000	—	—	40%
3.	Motor Buses & Lorries (used for hiring)	6,40,000	2,80,000	4,15,000	40%
4.	Imported car	3,30,000	—	—	—

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Calculate the amount of depreciation which firm can claim for the assessment year 1997-98 and also calculate the W.D.V. on 1.4.97. New Bus was brought into use from 1.12.1996 and Plant & Machinery on 1.7.1996.

Solution

Sr. No.	*Block of Assets*	*Depreciation Rs.*	*W.D.V./cost Rs.*
1.	*Plant & Machinery* – 25% Block		
	W.D.V. on 1.4.96		42,20,000
	Add: cost of additions made during the year		6,90,000
			49,10,000
	Less: scrap value of asset destroyed during the year		2,10,000
	Net W.D.V. on 31.3.97		47,00,000
	Depreciation on 31.3.97 @ 25%	11,75,000	11,75,000
	W.D.V. on 1.4.97		35,25,000
2.	*Plant and Machinery 40%*		
	W.D.V. as on 1.4.96		
	(*i*) Motor buses and lorries		6,40,000
	(*ii*) Aircraft		34,50,000
			40,90,000
	Add: Cost of new buses acquired and put into used on 1.12.96		2,80,000
			43,70,000
	Less: Money realised on discarding a bus		4,15,000
	W.D.V. of the block on 31.3.97		39,55,000
	Depreciation		
	On new bus used for less than 180 days (2,80,000 × 40% × 1/2)	56,000	
	On balance W.D.V. (36,75,000 × 40%)	14,70,000	
			15,26,000
	W.D.V. of the block as on 1.4.97		24,29,000
3.	*Imported car:* No depreciation is allowed on imported car unless it is used as taxi for running on hire	Nil	
	Total Depreciation	27,01,000	

7. Computation of depreciation in case of capital expenditure on a building taken on lease [Section 32(1A)]

In case an assessee is carrying on his business or profession in a building which is not owned by it but such assessee has incurred after 31.3.1970 some capital expenditure on additions, alterations or renovations in such hired building, assessee can claim the depreciation in the following manner:

(*a*) Depreciation is calculated on such expenditure at the rates prescribed for such type of building in the rate schedule.

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(*b*) In case any such structure or work is sold, discarded, demolished, destroyed or surrendered as a result of the termination of lease in respect of such building (but such event must take place in previous year other than the previous year in which such capital expenditure was incurred), the difference between written down value of such structure or work and money realised shall be allowed as depreciation of the year provided such deficiency is actually written off in the books of assessee.

8. Unabsorbed Depreciation [Section 32(2)]

With effect from assessment year 1997-98 unabsorbed depreciation shall be adjusted in following manner :

(*a*) It can be set off against the profits and gains of the business or profession for that assessment year.

(*b*) If any portion remains unadjusted it can be set off from any other income of the year.

(*c*) If still some portion of unabsorbed depreciation remains unadjusted it can be carried forward for 8 succeeding previous year to be set off only from *any income under the head profits and gains and not from any other head.*

(*d*) It is essential that the business whose depreciation is being carried forward must be continued in the year in which depreciation is being adjusted.

(*e*) The limit of 8 succeeding previous years shall not be applicable on a sick industrial company which is so declared under section 17 of Sick Industrial Company (Special Provisions) Act 1985 for the period between the previous year in which the entire networth of the company becomes equal to the accumulated losses.

9. Computation of Capital Gains/Loss in case of depreciable assets

In case assets are sold during the previous year and some gain occurs, this capital gain is taxable under the head "Capital Gain". Section 50 of the Income-tax Act provides the procedure for calculation of deemed Capital Gain/Loss in case of depreciable assets. This section provides for two situations:

1. Transfer of one or more assets in the block of assets [Section 50(1)]

Where the full value of the consideration received or accruing on transfer of one or more assets belonging to same block of assets exceeds the aggregate of the following amounts:

(*i*) Expenditure incurred in connection with such transfer;

(*ii*) The written down value of such block of assets at the beginning of previous year; and

(*iii*) The actual cost of any asset falling within that block of assets acquired during the year.

Such excess shall be deemed to be the short-term capital gain.

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2. Transfer of all the assets within same block of assets and block ceases to exist [Section 50(2)]

In such event the written down value of such block plus cost of any new asset acquired during the year is taken as actual cost and if it is less than total consideration received, the income if any as a result of such transfer or transfers shall be deemed to be short-term capital gain.

In case the W.D.V. of the block of assets and cost of new asset acquired during the year added together is more than the total consideration received, the difference is called Short-term Capital Loss.

Illustration 4. From the particulars given below, calculate the amount of depreciation, short-term capital gain or short-term capital loss (as the case may be):

		Rs.
(*i*)	W.D.V. of the block of P & M on 1.4.96	1,60,000
(*ii*)	Cost of additions made during May 1996	40,000
(*iii*)	Expenses incurred as commission etc. at the time of sale	10,000
(*iv*)	Net consideration of all the assets comprising in this block	2,40,000
	What difference it will make if the net consideration is	1,50,000

Solution

Computation of Capital Gain/Loss

		Rs.	Rs.
(*a*)	Net consideration received		2,40,000
	Less: W.D.V. of all assets on 1.4.96	1,60,000	
	Cost of new assets put into use during 1996-97	40,000	
	Expenses on transfer	10,000	
			2,10,000
	Short-term Capital Gains u/s 50(2) as the block of asset has ceased to exist and money realised is more than W.D.V. etc.		30,000
(*b*)	*If block of assets ceases to exist*		
	Net consideration received		1,50,000
	Less: W.D.V. of all assets on 1.4.96	1,60,000	
	Cost of new assets put into use during 1996-97	40,000	
	Expenses on transfer	10,000	
			2,10,000
	Short-term Capital Loss u/s 50(2)		60,000

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Q. No. 1

Mr. Ajay starts a new business on September 18, 1995. He acquired a plant A whose cost is Rs. 26,000 and rate of depreciation is 100%. He also acquired plant B for Rs. 30,000, rate of depreciation being 40% on March 31, 1996. On May 10, 1996 he sold plant A for Rs. 22,000 and plant B for Rs. 17,000. (Expenditure incurred in connection with transfer of plant A is Rs. 1,000. He however acquired following plants during the year 1996-97 :

Asset	*Date of Purchase*	*Cost*	*Rate of Dep.*
C	April 30, 1996	Rs . 6,000	100%
D	May 19, 1996	Rs. 12,000	40%
E	June 10, 1996	Rs. 21,000	25%

Compute the amount of depreciation and capital gain if any during previous year 1996-97. *[Punjab University B.Com.]*

[Hints : P & M 25% Block Dep. Rs. 5,250 P & M 40% Dep. Rs. 7,600 P & M 100% Block STC Gains Rs. 15,000]

II. INVESTMENT ALLOWANCE [Section 32A]

The Finance Act, 1976 has introduced a new scheme of investment allowance to replace the scheme of initial depreciation allowance. The new section 32A provides for the deduction of investment allowance while computing taxable profit under the head 'Business or Profession'. This new incentive of investment allowance is broadly designed on the lines of the scheme of development rebate that stands discontinued from 31.5.1974. It was replaced by Investment Deposit Account from 1.4.87 but has been reintroduced as an alternative to Investment Deposit Account with effect from assessment year 1989-90 and ***will not be available from 1.4.90 onwards.***

III. INVESTMENT DEPOSIT ACCOUNT

With effect from 1.4.87, *i.e.*, assessment year 1988-89, this scheme of Investment Deposit Account has been introduced replacing the old scheme of Investment Allowance. This deduction is allowed out of profits & gains of business or profession carried on by the assessee during relevant previous year. This new deduction is not linked with actual cost of new plant & machinery. It is linked with profits of the business and amount deposited in Investment Deposit Account or purchase of eligible plant & machinery.

The Finance Act 1990 has inserted a proviso according to which this deduction is ***not to be allowed with effect from assessment year 1991-92.***

IV. DEVELOPMENT ALLOWANCE [Section 33A]

The deduction of development allowance on the pattern of development rebate was introduced through the Finance Act of 1956. The Tea Finance Committee recommended this deduction taking into view the idea of increasing the areas under tea cultivation.

Section 33 A(1) says that a deduction of development allowance is to be allowed on the prescribed rates in respect of planting of tea bushes on any land in

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India owned by an assessee who carried on business of growing and manufacturing tea in India. Up to assessment year 1975-76, the deduction of development allowance was admissible only in respect of tea bushes planted on land owned by the assessees. The Finance Act, 1975 has amended section 33 A and thus extending the benefit of this deduction in case of tea bushes planted or replanted on land which is not owned by the assessee but also that land in respect of which he has a leasehold or other right of occupancy. This amendment was given effect retrospectively from 1st April 1965, *i.e.*, assessment year 1965-66 and subsequent years.

Rates. (*i*) Where the tea bushes have been planted on any land not planted at any time with tea bushes or on land which has been previously abandoned—50% of the actual cost of planting.

(*ii*) Where tea bushes are planted in replacement of tea bushes that have died or have become permanently useless on any land already planted—30% of the actual cost of planting.

According to Finance Act 1990 this deduction will not be allowed from assessment year 1991-92.

V. TEA DEVELOPMENT ACCOUNT [Section 33AB]

In case an assessee has deposited a certain amount in a special account with a national bank, he shall be allowed this deduction. The assessee must be engaged in the business of growing and manufacturing tea.

Rate of Deduction [33 AB(i)]

(*i*) Amount deposited in a special account with National Bank;

Or

20% of profits from such business (computed under the head. "Profits & Gains of Business or Profession" before allowing this deduction).

Whichever is less is allowed as deduction out of the profits of the year before adjusting the brought forward losses. In case assessee has claimed a deduction in respect of a deposit in one previous year it will not be allowed in any subsequent previous year. In case deduction is claimed by the firm, it shall not be allowed to its partners again.

Special Account defined. It is an account to be opened with National Bank for Agriculture and Rural Development (NABARD).

The Finance Act 1994 has extended this benefit for any deposit made in an Account called TEA DEPOSIT ACCOUNT opened by the assessee in accordance with and for the purposes specified in a scheme framed by the Tea Board with the prior approval of Central Government. This benefit is to be made available only in relation to assessment years 1995-96 and afterwards.

When to deposit. Amount has to be deposited:

(*a*) before the expiry of six months from close of previous year; or

(*b*) before date of furnishing of return; whichever is earlier.

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Withdrawal of Amount [Section 33AB(3)]

Withdrawal from this account will not be allowed except on:

(*a*) closure of Business;
(*b*) death of an assessee;
(*c*) partition of H.U.F.;
(*d*) dissolution of firm; or
(*e*) liquidation of company.

In case any amount is withdrawn due to closure of business or dissolution of firm, before 8 succeeding previous years the whole of such amount shall be deemed as income taxable under the head Profits & Gains of business or profession of the previous year in which amount is withdrawn [33 AB(5)].

In case any amount is withdrawn and utilised for the business during any previous year such expenditure shall not be debited to Profit & Loss Account of that previous year [33 AB(6)].

In case any amount is released by the Bank in connection with a scheme approved by Bank (NABARD) such amount must be utilised within same previous year. Any amount remaining unutilised is deemed as income taxable under Profits & Gains of business or profession [33 AB(7)].

Compulsory Audit. In case of an assessee who is not subject to audit under any provision of Income-tax Act, and such assessee wants to claim this deduction, it must get its accounts audited and the report of such audit must accompany the return [33 AB(2)].

No deduction. No deduction shall be allowed in respect of any amount utilised for the purchase of:

(*a*) any plant & machinery installed in office premises, residential houses and Guest houses;
(*b*) any office appliances (except computers);
(*c*) any plant & machinery whose full actual cost has been allowed as deduction;
(*d*) any new plant & machinery installed for production of an article specified in 11th schedule [33 AB(4)].

Deemed Profit. In case an asset acquired under this scheme is sold/transferred before expiry of 8 succeeding previous years, the amount of cost which was met out, amount released from special account shall be deemed to be profit & gain from the business [33 AB(8)].

VI. RESERVES FOR SHIPPING BUSINESS [Section 33AC]

With effect from assessment year 1990-91, the Direct Tax Laws (Second Amendment) Act, 1989 has inserted this new section. The provisions of this new section are:

Rate of Deduction [33AC(1)]. Deduction of an amount not exceeding 50% of the total income (computed before making any deduction under this section and u/s 80) as is debited to the profit and loss account of the previous year in respect of which the deduction is to be allowed shall be admissible.

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Eligibility. The deduction shall be admissible only to a *Govt. Company or public company formed and registered in India* with the main object of carrying on the business of operation of ships.

Restriction on deduction

The amount of deduction to be claimed must be transferred to a Reserve account. The amount to be credited to such reserve account must not exceed twice the amount of the paid-up share capital (excluding the amounts capitalised from reserves) of the assessee company. In the year in which the reserve exceeds this limit deduction u/s 33AC will be restricted to the amount which is sufficient to reach this limit.

Use of Reserve [33AC(2)]

The amount credited to the reserve account shall be utilised by the assessee company before the expiry of *8 succeeding* previous years for

(*a*) acquiring a ship for the purposes of the business of assessee; and

(*b*) until the acquisition of a new ship, such reserve may be utilised for the business of the assessee but not for distribution by way of dividends or profits or remittance outside India as profits or for the creation of any asset outside India.

Non-Utilisation of Reserve [33AC(3)]

In case amount of reserve is not utilised in the aforesaid manner the amount of reserve shall be treated in the following manner:

(*a*) In case amount is utilised for a purpose other than as given above, the amount so utilised for other purpose shall be deemed as profit of the previous year in which it is so utilised.

(*b*) In case amount of reserve is not utilised to acquire a ship within 8 succeeding previous years, the amount so unutilised shall be deemed as income of the previous year next following the period of 8 succeeding previous years.

(*c*) In case ship is acquired within 8 succeeding previous years, it cannot be sold or otherwise transferred for 8 succeeding previous years from the previous year in which it is acquired. In case it is sold or transferred before the expiry of 8 succeeding previous years, the amount of reserve utilised in acquiring the ship shall be deemed as profit of previous year in which ship is sold or transferred.

COMPUTATION OF DEPRECIATION, INVESTMENT DEPOSIT ACCOUNT AND DEVELOPMENT ALLOWANCE

Item	*Treatment*
I. Depreciation Section—32	
1. Definition:	Normal wear and tear of the assets owned by assessee used in business or profession during the previous year. The asset may be used at any time during the year. If used for less than 180 days only 50% of depreciation to be allowed.

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Item	*Treatment*
2. **Asset:**	Building, machinery, plant and furniture. Plant includes ships, vehicles, books, scientific apparatus, surgical equipment, sanitary and pipe-line fittings of hotel, and service lines, switch gears etc. of electric supply company.
3. **Allowance:**	Deduction of depreciation is to be allowed at the prescribed rates out of the profit of previous year. It is allowed on written-down value basis in case of all assets. No depreciation is allowed in the year in which asset is sold, demolished, destroyed or discarded. Actual cost means the cost at which asset was first acquired and if acquired before 1.4.81 the assessee is given the option to opt for W.D.V. or F.M.V. as existing on 1.4.81 for depreciation.

II. New Method of Depreciation

With effect from 2.4.87 new method of depreciation has become applicable. It provides for new concept of block of assets, new higher rates, only one type of depreciation, short-term capital gain or loss instead of Balancing charge or terminal depreciation.

1. **Block of assets**	U/s 2(11) Block of assets means the group of assets falling within a class of assets in respect of which the same rate of depreciation has been prescribed.	
2. **New rates of depreciation**	All assets have been dividend into 4 groups.	
	Group I: Buildings	
	(*a*) Ordinary residential buildings	5%
	(*b*) Factory buildings	10%
	(*c*) Hotel buildings or small residential houses	20%
	(*d*) Temporary structures	100%
	Group II: Furniture	
	(*a*) General rate	10%
	(*b*) Furniture of Hotel, School, Libraries etc.	15%
	Group III: Plant & Machinery	
	(*a*) General Rate on All P & M including cars and scooters	25%
	(*b*) Cars acquired on or after 1.4.90	20%
	(*c*) Lorries, Buses, Taxies etc. and water & air pollution control equipment	40%
	(*d*) Energy saving devices or solar energy equipment etc.	100%
	(*e*) Books required for professional use	100%
	Group IV: Ships	
	(*a*) Ships (ocean-going)	20%
	(*b*) Inland vessels (speed boats)	10%
	(*c*) Other inland vessels	20%
3. **Actual cost of assets:**	(*i*) Cost actually met by assessee (*i.e.* cost less Govt. subsidy etc.)	
	(*ii*) Actual cost to include cost of installation, expenses on insurance, freight, loading and unloading expenses on modification and repairs before use of asset, interest paid on acquiring the asset before asset has been put into use.	

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(*iii*) Cost of cars imported into India after 28.2.75—No depreciation is allowed. For Cars acquired between 1.4.67 to 28.2.75 cost was deemed as Rs. 25,000 if higher cost was paid.

(*iv*) Asset used for scientific research but converted into business asset—actual cost of asset less any amount allowed as deduction in respect of it.

(*v*) Asset acquired by way of gift or inheritance—the W.D.V. of previous owner is taken as cost of present assessee.

4. **Method of depreciation:** On all assets (including ocean-going ships) the depreciation is to be calculated on written down value basis.

5. **W.D.V.** (*a*) *In case of assessment year 1988-89*

(*i*) W.D.V. (aggregate) of all the assets falling within same block as on 1.4.87.

(*ii*) Add actual cost of any new asset of same group acquired (put into use) during the year.

(*iii*) Deduct any amount received on account of sale, demolition, discarding or destruction of any asset during the year. Resultant amount shall be the W.D.V. for the purpose of calculation of depreciation.

(*b*) *In case of assessment year 1989-90 and afterwards*

(*i*) Out of the amount calculated at (*a*) above deduct the amount of depreciation actually allowed during the year.

(*ii*) repeat the points (*ii*) and (*iii*) given above to get W.D.V. for further depreciation.

6. **Computation of depreciation** Depreciation = W.D.V. of block × rate for such block/100.

7. **Unabsorbed depreciation:** In case available profit is less than admissible depreciation, the unadjusted portion is called unabsorbed depreciation which is added to the succeeding previous year's depreciation and is treated as current depreciation of such succeeding previous year and so on.

8. **Short-term capital gain** [Section 50] (*a*) *Transfer of one or more assets*—Short-term Capital Gain = Total consideration Less

(*i*) W.D.V. of such block of assets;

(*ii*) Exp. incurred on such transfer;

(*iii*) Actual cost of any asset acquired during the year belonging to same block.

(*b*) *Transfer of all the assets in same block*—Out of total consideration received less actual cost or W.D.V. of all the assets and actual cost of any new asset acquired during the year is deducted and difference is called Short Term Capital Gain/ Loss as the case may be.

III. Investment Allowance [Section 32 AB]—Discontinued from 1.4.90.

IV. Investment Deposit Account [Section 32AB]—Discontinued from 1.4.90.

V. Development Allowance [Section 33 (A)]—Discontinued from 1.4.90.

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Illustration 5. The following are the fixed assets owned and used by a firm in its business of manufacturing pesticides for the assessment year 1997-98:

	Block of Asset	*W.D.V. on 1.4.96* Rs.	*Additions during the year* Rs.	*Rate of Dep.*
(*i*)	Factory building	8,00,000	1,00,000 [Completed on 1.1.97]	10%
(*ii*)	Residential building	3,00,000	50,000 [Completed on 1.5.96]	5%
(*iii*)	Plant and machinery (General)	50,00,000	10,00,000 [Installed on 15.6.1996]	25%
(*iv*)	Furniture and fittings	1,00,000	—	10%

Calculate the total amount of depreciation.

Solution. ***Calculation of Depreciation***

Block of Asset	*Cost/W.D.V.* Rs.	*Rate*	*Depreciation* Rs.
(*i*) Factory Building			
W.D.V. on 1.4.96	8,00,000		
Additions on 1.1.97 (used for less than 180 days)	1,00,000		
	9,00,000	(10% of Rs. 8,00,000)	80,000
		(5% of Rs. 1,00,000)	5,000
(*ii*) Residential Building			
W.D.V. on 1.4.96	3,00,000		
Additions on 1.5.96	50,000		
	3,50,000	5%	17,500
(*iii*) Plant & Machinery			
W.D.V. on 1.4.96	50,00,000		
Additions on 15.6.96	10,00,000		
	60,00,000	25%	15,00,000
(*iv*) Furniture & Fitting			
W.D.V. on 1.4.96	1,00,000	10%	10,000
Total Depreciation			16,12,500

Illustration 6. An Iron and Steel Mill purchased a plant in the year 1995-96 for Rs. 8,00,000 out of which Rs. 2,00,000 was received from the Govt. of India.

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The plant was destroyed by fire in November 1996 and insurance company accepted a claim of Rs. 3,00,000 and the scrap was sold for Rs. 10,000.

Work out the amount of depreciation or other claim for the previous years 1995-96 and 1996-9.7 If (*a*) grant was given to meet the cost of plant ; or (*b*) as an incentive to set up industry in a backward area.

Solution

(*a*) *If grant is given to meet the cost of plant*

		Rs.
Purchase price of the plant in 95-96		800,000
Less grant received		200,000
Actual Cost u/s 43 (1)		600,000
Depreciation on 31.3.96 @ 25%		1,50,000
WDV on 1-4-96		4,50,000
Less money realised		
Insurance Claim	Rs. 300,000	
Scrap Value	Rs. 10,000	
		3,10,000
Short Term Capital Loss		1,40,000

(*b*) *It grant is given as an incentive*

	Rs.
Purchase Price of the Plant	8,00,000
Grant received from Government	Nil
Not to be deducted [C.I.T. v. P. J. Chemicals Ltd. (SC)]	
Actual Cost of the Plant to the Assessee	8,00,000
Depreciation @ 25% for Accounting year 1995-96	2,00,000
W.D.V. on 1.4.96	6,00,000
Deduct the amount of the Insurance Claim accepted by the Insurance Co. and Scrap value [3,00,000 + 10,000 = 3,10,000]	3,10,000
Short-term Capital Loss U/s 50	2,90,000

Note: Due to destruction of the asset which consisted of one full block, the difference between W.D.V. on 1.4.96 and money realised on account of insurance claim and scrap value, is called short-term capital loss and is treated under the next head "Capital Gains" u/s 50.

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Illustration 7. Calculate the amount of depreciation on the assets of a mill from the following particulars:

Block of Asset	*W.D.V. on 1.4.96* Rs.	*Additions made on 1.6.96* Rs.	*Rate of Depreciation*
(*i*) Factory building	14,00,000	6,00,000	10%
(*ii*) Residential building	4,00,000	1,00,000	20%
(*iii*) Plant and Machinery	30,00,000	10,00,000	25%
(*iv*) Furniture	25,000	—	10%
(*v*) Cars (acquired before 1.4.90)	65,000	—	25%

The factory building which was destroyed by fire, for that insurance company accepted the claim for Rs. 60,000 and scrap value realised amounted to Rs. 10,000. Residential building consists of residential units whose plinth area does not exceed 80 sq. metres each.

Solution

Calculation of Depreciation

Sr. No.	*Block of Asset*	*W.D.V./Cost* Rs.	*Rate*	*Depreciation* Rs.
1.	Building (Factory)			
	W.D.V. on 1.4.96	14,00,000		
	Add: Additions [1.6.96]	6,00,000		
		20,00,000		
	Less: Money realised	70,000		
		19,30,000	10%	1,93,000
2.	Residential Building			
	W.D.V. on 1.4.96	4,00,000		
	Add: Additions [1.6.96]	1,00,000		
		5,00,000	20%	1,00,000
3.	Plant & Machinery			
	W.D.V. on 1.4.96	30,00,000		
	Motor Car W.D.V. on 1.4.96	65,000		
	Add: Additions [1.6.96]	10,00,000		
		40,65,000	25%	10,16,250
4.	Furniture			
	W.D.V. on 1.4.96	25,000	10%	2,500
			Total Depreciation	13,11,750

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Ilustration 8. Mr. Puneet Kansal, an advocate, acquired following assets during the year 1996-97 :

Asset	*Date of acquisition*	*Cost*	*Rate of Dep.*
(*i*) Computer with printer	1.11.96	60,000	25%
(*ii*) Office Almirah	1.4.96	4,200	10%
(*iii*) Electronic Typewriter	1.7.96	12,500	25%
(*iv*) Office Table and Book Stand	1.4.96	20,000	10%
(*v*) Books	During the year	60,000	100%

Calculate the amount of depreciation for the year 1996-97 and W.D.V. of the assets as on 1.4.97. His professional income for the year was only Rs. 30,500 and under other sources was Rs. 16,400. How the depreciation will be adjusted ?

Solution. *Computation of depreciation for the previous year 1996-97*

Asset	*Rs.*	*Rs.*
1. *Furniture 10% Block*	W.D.V.	Dep.
(*i*) Office Almirah	4,200	
(*ii*) Office Table and Book Stand	20,000	
Cost on 31.3.97	24,200	
Depreciation @ 10%	2,420	2,420
W.D.V. on 1.4.97	21,780	
2. *Plant and Machinery 25% Block*		
Cost of Computer and Printer on 1.11.96	60,000	
Cost of electronic typewriter on 1.7.96	12,500	
Cost on 31.3.97	72,500	
Depreciation		
(*i*) On computer used for less than 180 days (60,000 × 25% × 1/2)		7,500
(*ii*) On typewriter used for more than 180 days (12,500 × 25%)	10,625	3,125
W.D.V. on 1.4.97	61,875	
3. *Books for professional use—100% Block*		
Cost of Books	60,000	
Depreciation @ 100%	60,000	60,000
Total Depreciation		73,045
Adjustment of Depreciation		
Profit and gains		
Professional Gain	30,500	
Less depreciation	73,045	
Unadjusted Depreciation	42,545	Nil

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Income from other sources	
Other Incomes	16,400
Gross total income	16,400
Unadjusted depreciation to be adjusted from G.T.I.	42,545
Unabsorbed depreciation to be carried forward	26,145

Q. N. 2

Goodluck Ltd. purchased a plant for Rs. 40,00,000 from Raj Udyog Ltd. and received Rs. 5,00,000 by way of subsidy from the Government for the *purchase of plant* during the financial year 1995-96. In January, 1997 the plant was completely destroyed in fire and a claim of Rs. 4,00,000 was settled by the Insurance Company. The scrap was sold by the company for Rs. 70,000. Assuming that plant is depreciable at 25%, compute depreciation etc. for the previous years 1995-96 and 1996-97 in the following cases.

(*a*) If the plant is replaced in February, 1997 at a cost of Rs. 45,00,000.

(*b*) If the plant is not replaced. [*B.Com.P.U.*]

(**Hints :** Subsidy shall be reduced from cost as it is given specifically to meet the cost of asset.

(*a*) Depreciation in previous year 1995-96 Rs. 8,75,000 and in 1996-97 Rs. 11,01,250 ;

(*b*) Depreciation in previous year 1995-96 Rs. 8,75,000 and short term capital loss in 96-97 Rs. 21,55,000]

Q. No. 3

B purchases on 30 April, 1996 a new machine at a cost of Rs. 1 lakh. In bringing it to factory site he incurs expenses on clearing, freight and loading and unloading amounting to Rs. 5,000, Rs. 1,000 and Rs. 500 respectively. In installing the machine a further cost of Rs. 10,000 is incurred. It is then found that a part is broken and in repairing such broken part an additional expenditure of Rs. 7,500 becomes necessary. Ultimately on 31 January, 1997 the machinery is ready for use and is actually brought into use on that day. If the rate of depreciation is 25%, determine the actual cost of the machinery for purposes of depreciation and also the amount of depreciation admissible for the assessment year 1997-98 and W.D.V. on 1.4.97. The previous year ends on 31 March, 1997. Give reasons for your answer. *[B.Com. Calcutta]*

[Hints: Actual cost Rs. 1,24,000; Normal Depreciation @ 25% but allowed one half as used for less than 180 days Rs. 15,500; W.D.V. on 1.4.97 Rs. 1,08,500]

Q. No. 4

A machine purchased in 1995 for Rs. 80,000 was brought into use on 31 October, 1995 after installation at a cost of Rs. 10,000. The assessee's accounting period for the relevant business is the financial year. On 30 June, 1996 the machine was destroyed by fire and the scrap was sold for Rs. 500, the fire insurance people

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paying a further sum of Rs. 54,500. The rate of depreciation is 25% for assessment year 1996-97. This machinery was only item of this block. Calculate the W.D.V. on 1.4.96 and the claim which assessee can make for the assessment year 1997-98.

[**Hints:** W.D.V. on 1.4.96 Rs. 78,750. Short term Capital Loss Rs. 23,750]

Q. No. 5

From the following particulars you are required to ascertain the depreciation admissible and other liabilities in respect of the previous year relevant to assessment year 1997-98 :—

	P & M	*Building*
	Rs.	Rs.
Written down value at the beginning of year	2,50,000	10,00,000
Additions during year	3,00,000	Nil
Sales during year	6,00,000	2,00,000

Rate of depreciation for P & M is 25% and Building is 10%.

[Adapted C.A. Inter May 1995]

[**Hints** : Plant & Machinery 25% Block, STCG Rs. 50,000 Building 10% Block, Dep Rs. 80,000]

Q. No. 6

The following are the particulars of assets at the beginning of the year:

	W.D.V. on 1.4.96	*Rate*
1. Building (Non-Residential)	10,00,000	10%
2. Building (Residential)	5,00,000	5%
3. Furniture	1,00,000	10%
4. Plant and Machinery	15,00,000	25%
5. Motor Cars (acquired before 1.4.90)	1,00,000	25%
6. Trucks	25,000	25%
7. Electric Fans	2,000	25%

Machinery worth Rs. 5,00,000 was purchased and installed on 14.10.96. One machine was sold for Rs. 45,000 during the year. The assessee is engaged in the business of manufacturing fertilizers using Indian technical know-how.

One residential building was destroyed by fire during the year for which insurance company accepted a claim for Rs. 60,000.

Calculate the amount of depreciation for the previous year ending on 31.3.1997.

[**Hints:** Block Non-residential Building Depreciation Rs. 1,00,000; Block Residential Building Depreciation Rs. 22,000; Block Furniture Depreciation Rs. 10,000; Block P & M Depreciation Rs. 4,58,000: Total Depreciation Rs. 5,90,000]

Q. No. 7

From the following particulars of Fixed Assets of West Bengal Paper Mills Ltd., you are required to work out the amount of depreciation allowable.

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Fixed Assets	*W.D.V. on 1.4.96* Rs.	*Additions during the year* Rs.	*Rate of Depreciation*
Building (Non-Residential)	10,20,000	Nil	10%
Building (Residential)	2,25,000	Nil	5%
Plant and Machinery	30,28,200	4,30,000	25%
Motor Cars (acquired before 1.4.90)	65,000		25%
Furniture	18,300	Nil	10%

Part of the Residential building was completely destroyed by fire on 5.6.96 and Rs. 95,000 was received from the insurance company in respect thereof.

The additions to the Plant and Machinery and Motor Vehicles were all new and installed on 1.10.96. *[Adapted I.C.W.A.]*

[Hints: Factory Building Rs. 1,02,000; Non-Factory Building Rs. 6,500; Furniture Rs. 1,830; P & M Rs. 8,80,800] [P-1.]

Q. No. 8

From the particulars given below, compute the depreciation and other claims for the assessment year 1997-98:

Sr. No.	*Assets*	*Actual Cost* Rs.	*W.D.V. on 1.4.96* Rs.	*Rate of Dep.*
1.	Factory Building			
	I	8,00,000	4,50,000	10%
	II	6,00,000	80,000	10%
2.	Plant & Machinery			
	A	2,10,000	1,50,000	25%
	B	4,00,000	2,00,000	25%
	C	5,60,000	3,10,000	40%
	Following new additions were made during the month of June 1996:			
1.	Building III	4,00,000	—	10%
	Building IV	2,80,000	—	5%
2.	Plant & Machinery D	8,00,000	—	25%
	Plant & Machinery E	1,60,000	—	40%

Following assets were sold during the previous year:

1. Building	II	Net consideration	Rs. 5,00,000
2. Plant	B	Net consideration	Rs. 8,50,000
3. Plant	C	Net consideration	Rs. 5,00,000

[Hints: 1. W.D.V. of Factory Building Block on 31.3.97 Rs. 4,30,000 Depreciation 43,000.

2. W.D.V. of Non-Factory Building Block on 31.3.97 Rs. 2,80,000 Depreciation 14,000.

3. W.D.V. of P & M (25%) Block on 31.3.97 Rs. 3,00,000 Depreciation 75,000.

4. W.D.V. of P & M (40%) Block on 31.3.97 Rs. 4,70,000. Short-term capital gain Rs. 30,000]

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Q. No. 9

Calculate Depreciation on the following assets:

Assets	*W.D.V. on 1.4.96* Rs.	*Rate of Depreciation*
Building A	4,25,000	5%
Building B	3,65,000	10%
Building C	4,10,000	10%
Furniture	20,810	10%
Plant and Machinery A	5,30,000	40%
Plant and Machinery B	2,10,000	25%

Following assets have been purchased & installed during the previous year 1996-97 on 10.11.96 but plant "C" was acquired in April 1996.

Assets		*Actual Cost* Rs.	*Rate of Depreciation*
Plant	C	1,08,000	100%
Plant	D	2,40,000	40%
Plant	E	3,40,000	25%
Building	D	4,00,000	10%
Building	E	1,00,000	5%

Following assets have been sold during the previous year.

		Sale Consideration
Building	B	5,25,000
Plant	A	2,70,000

Rs. 75,000 were also spent to renovate and modify Building A. Rs. 1,00,000 has also been spent on Machinery B to make it suitable for the new system of production.

[**Hints:** Depreciation on Building (5%) Rs. 27,500, Building (10%) Rs. 45,000, Furniture Rs. 2,081, P & M (25%) Rs. 1,20,000 P & M (40%), Rs. 1,52,000 P & M (100%) Rs. 1,08,000. Total Depreciation Rs. 4,54,581] [P-6].

QUESTIONS

1. What do you mean by the term depreciation? What are the rules regarding the claim of deduction of depreciation?
2. Write in brief the new method of charging depreciation.
3. Explain the provisions of claim of deduction of Tea Development Account and Reserve for Shipping Business.
4. Write notes on:
   (*a*) Unabsorbed Depreciation
   (*b*) Short-term capital gain/loss on depreciable assets.
   (*c*) Depreciation on capital expenditure incurred on buildings taken on lease.
   (*d*) W.D.V. u/s 43 (6).
5. Discuss the concept of 'actual cost' as given u/s 43 (1).

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5 CAPITAL GAINS

Scope of charge—Capital asset—Basis of charge—Transfer of capital asset—in the previous year—deemed transfer—transfer not regarded as transfer—Computation of Capital Gain (New method)—Cost of acquisition—Exempted capital gains—Treatment of capital losses—Deduction u/s 48(2)—Chart—Illustrations—Questions.

This is the fourth head of income chargeable to tax as given in section 14. First of all this income was made chargeable to tax in 1947 and contained the transfer made up to and on 31st March 1948. This charge was abolished from 1.4.1948 onward but it was revived from the assessment year 1957-58 and income accruing from all transfers effected after 31st March 1956 was made chargeable to tax under this head.

Scope of Charges

(*a*) **Capital Asset.** The tax is to be levied on any profit or gain occurring on the transfer of a capital asset. Section 2(14) defines capital assets as: "property of any kind held by an assessee whether or not connected with his business or profession".

This definition has a very wide coverage as it includes all types of properties, whether movable or immovable, tangible or intangible, fixed or floating. Such asset may represent not only actual ownership but also any right in relation to any property which is capable of being transferred. The goodwill, the lease-hold rights, right to subscribe for shares and share of partner in partnership etc. are also considered as capital assets for the purpose of this head. In case a person transfers his tenancy rights to another person, it has been held that it is a self-generating asset and is not eligible to tax under capital gains. *[C.I.T. v. B.C. Srinivasa Shetty (S.C.)]* and *C.I.T. v. Mrs. Shrinbhiai P. Pandale [(Bombay)]*. With effect from 1.4.1973 jewellery is also included in the term 'capital assets'. Even a licence obtained by the assessee from the Government to start some manufacturing activity shall be included in this term.

(*b*) **What is not included in Capital Asset?** Under Section 2(14) following assets have been specially excluded from the scope of the definition of capital assets:

(*i*) Any stock-in-trade, raw materials, consumable stores held by any assessee for the purposes of his business or profession.

(*ii*) Personal effects (movable property) including wearing apparel, motor car, electrical appliances, refrigerator, furniture etc.; ornaments excluding jewellery held for personal use by the assessee or any other member of his family dependent upon him.

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Explanation: The Capital Gain on transfer of jewellery is fully taxable and as such it is necessary to understand the meaning of term 'jewellery'. According to explanation attached to Section 2 (14) (ii) the term "jewellery" includes:

(*a*) ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals whether or not containing any precious or semi-precious stone and whether or not worked or sewn into any wearing apparel;

(*b*) precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel.

(*iii*) Agricultural Land in rural India—*But the land should not be situated* within the limits of any municipality or cantonment board having a population of 10,000 or more or situated in areas within distance not exceeding 8 kms from the local limits, if such areas are notified by the Central Government for the urbanisation or other relevant considerations.

(*iv*) 6% Gold Bonds 1977 or 7% Gold Bonds 1980 or National Defence Gold Bonds, 1980 issued by the Central Government.

(*v*) Special Bearer Bonds, 1991.

(*c*) **Types of Capital Assets.** For computing capital gains, assets have been divided into two categories:

(*i*) *Short-term capital assets* [Section 2 (42-A)]. Short-term capital asset is that which is held by an assessee for not more than 36 months immediately preceding the date of its transfer.

In the case of shares held in a company the period has been reduced to 12 months with effect from 1.4.88 *i.e.*, assessment year 1988-89.

With effect from assessment year 1995-96, the securities listed is any recognised stock exchange, units of U.T.I. and units of Mutual Funds shall be treated as Long Term capital assets if held for 12 months or more.

In case an assessee subscribes to right issue himself, or subscription is made by renouncee the period shall be counted from the date of allotment of such financial asset.

In case subscription is made against the right being renounced in favour of any other person the period will be counted from the date on which offer is made by the company or financial institution.

Any gain or loss accruing to the assessee on such assets shall be known as short-term capital gain or loss. [2(42B)].

(*ii*) *Long-term capital assets.* Assets which do not fall within the definition given in section 2(42), *i.e.*, the assets which are held by the assessee for a period exceeding 36 months immediately preceding the date of transfer, are called 'long-term capital assets'.

Any gain or loss accruing on such asset shall be known as long-term capital gain or loss. [2(42B)].

The period to determine the nature of such assets which are acquired under transfers not regarded as transfers, shall be taken to the total period for which asset

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was held by previous owner and the present owner, *e.g.*, Mr. A acquired an asset on 15th January 1984 and gifted it to his son, D on 31st Dec., 1985, D sold it on 20th Feb., 1993. The transfer from A to D is not to be regarded as transfer u/s 47(*iii*) and it is a long-term capital asset as it was held by Mr. A and Mr. D together, for more than 36 months.

Basis of Charge [Section 45]

U/s 45(1) any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in section 54, be chargeable to income-tax under the head 'capital gains' and shall be deemed to be the income of the previous year in which the transfer took place.

The above definition can be split up into two parts:

(*a*) *Income arising from the transfer* of a capital asset

(*b*) *Effected in the previous year*

and it is essential to study both the parts in detail.

Transfer of a Capital Asset

(*a*) *Transfer*—U/s 2(47) of Income-tax Act 1961, the term 'transfer' has been defined as:

Transfer in relation to a capital asset includes:

(*i*) the sale, exchange or relinquishment of the asset; or

(*ii*) the extinguishment of any rights therein; or

(*iii*) the compulsory acquisition thereof under any law; or

(*iv*) in a case where the asset is converted by the owner thereof into, or is treated by him as stock-in-trade of a business carried on by him, such conversion or treatment; or

(*v*) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882; or

(*vi*) any transaction (whether by way of becoming a member of, a acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring or enabling the enjoyment of, any immovable property.

In this definition the word 'transfer' represents the sale, exchange or relinquishment of the assets. The ownership of the asset has to change to make a complete transfer. Eric L. Kohler has defined transfer as "The passage of property usually with title, or of services from one person to another." The asset may be transferred under free-will or under compulsion. The scheme of capital gain taxation includes both the types of transfer, voluntary or involuntary. As such any sale of asset of debtor under the court order will be 'transfer' under the provision of this Act.

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It is immaterial whether the assets are transferred by the owner himself or on his behalf by some other person. Assets of the firm under dissolution are sold by a commissioner or receiver under the order of court and if there is capital gain, the firm under dissolution will pay tax on such capital gain.

The compulsory acquisition of an asset by Government also constitutes 'transfer' and any gain arising from such transaction will also be considered as 'Capital Gains'. The meaning of word 'transfer' is not restricted only to transfers by act of parties: compulsory acquisition of the property also amounts to a transfer. *[Vadilal Soda Ice Factory v. CIT (1917) 80 I.T.R. 711].* "A running concern's sale by a firm to a company (newly formed) will also be considered as transfer."

In the Previous Year

The capital gain is deemed to be the income of the previous year in which the transfer takes place. As such any capital gain should be assessed in the assessment year corresponding to the previous year in which transfer took place.

A transfer does not take place merely because an agreement has been entered into or consideration is paid thereunder in whole or in part. The words "effected in the previous year" in section 45 denote that the title in the property has passed from the transferor to the transferee. No transfer can be said to be effected till all the formalities for transferring the title to the transferee are not completed.

The following rules can be framed in this connection:

(*i*) In respect of transaction concerning immovable property worth Rs. 100 or above, no capital gain can be charged to tax so long as there is no registration deed or transfer—though possession might have been given to the buyer.

(*ii*) The charge of capital gain arises only when there has been a duly executed and registered deed of transfer.

(*iii*) The year of assessment would be the year corresponding to the previous year in which such transfer is completed.

(*iv*) Whether the consideration is paid at the time of transfer or made payable in future, is immaterial, the charge will be levied in the year in which transfer of title takes place.

Deemed Transfer [Section 45(2)]

In case a capital asset is converted into stock-in-trade, or is treated as stock-in-trade by the assessee it will be deemed to have been transferred. The difference between market value and the cost price shall be taxable as capital gain under this head.

Transfer of Capital Assets by a person to Firm, AOP or Body of Individuals [Section 45 (3)]

When a person transfers his capital asset to a firm, AOP or body of Individuals in which he is or becomes partner or member by contributing capital or otherwise, profit or gain from such transfer shall be chargeable to tax as his income of the previous year in which such transfer takes place and for computation of capital gain, the amount recorded in the books of firm, AOP or body of individuals as the value

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of capital asset shall be deemed as full consideration for transferor. This provision has come into effect from 1.4.88 *i.e.* assessment year 1988-89.

The amount recorded in the books of firm, BOI or AOP, shall become sale price. The cost at which it was acquired by the person shall be treated as cost of acquisition.

Transfer of Capital Assets on dissolution of firm, AOP or Body of Individuals [Section 45 (4)]

When an asset is transferred by way of distribution on the dissolution of firm, AOP or body of individuals, the profit or gain arising from such transfer, shall be chargeable to tax as the income of firm, AOP or body of individuals, of the previous year in which such transfer takes place.

For computing capital gains the Fair Market Value on the date of transfer shall be deemed to be the full value of the consideration received or accruing as a result of the transfer. This provision has come into effect from 1.4.88 *i.e.* assessment year 1988-89.

The amount recorded in the books of firm, BOI or AOP shall be the cost of the asset and the fair market value on the date of transfer to the person shall be treated as sale price.

Enhancement of Compensation on Compulsory Acquisition of Assets [Section 45 (5)]

In case of compulsory acquisition of assets if the consideration is determined or is approved by Central Govt., or the Reserve Bank of India and later on such consideration is enhanced by the Court or Tribunal, the Capital Gain shall be treated in the following manner:

(*a*) the capital gain arising due to such acquisition shall be taxable in the previous year in which transfer takes place;

(*b*) the enhanced compensation or consideration shall be chargeable to tax under the head "Capital Gains" of the previous year in which such amount is received by the assessee (or by any other person, if original transferor has died).

This provision has come into effect from 1.4.88 *i.e.* assessment year 1988-89.

Sale of Units purchased for deduction u/s 80CCB [45(6)]

The difference between the repurchase price of the units purchased for deduction u/s 80 CCB and the capital value of such units shall be deemed to be the capital gain arising to the assessee in the previous year in which such repurchase takes place.

Capital value of such units means any amount invested by the assessee in the units eligible for deduction u/s 80CCB.

Transactions not regarded as transfer. Under Section 47, the following transactions are not regarded as transfers. Hence any gain arising from such transactions is also not taxable under the head 'Capital Gains'.

(*i*) Any distribution of capital asset on the total or partial partition of Hindu Undivided Family.

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But this provision will not be applicable if the assets of the HUF are sold by Karta and cash is realised and after that the cash is distributed among the members. In this case HUF shall have to pay tax on any gain which has accrued to it on sale of assets.

(*ii*) Omitted.

(*iii*) Any transfer of assets under a gift or will or an irrevocable trust.

(*iv*) Any transfer of capital assets by a company to its subsidiary company, if

(*a*) The parent company or its nominees hold the whole of share capital of the subsidiary, and

(*b*) The subsidiary company is an Indian company.

(*v*) Any transfer of capital assets by a subsidiary company to the holding company, if

(*a*) The whole of the share capital of the subsidiary company is held by the holding company, and

(*b*) The holding company is an Indian company.

The Finance Act 1988 has added an explanation according to which the provisions of points (*iv*) and (*v*) above shall not be applicable if an asset is converted into stock-in-trade. This provision is applicable from 29th Feb. 1988.

(*vi*) Any transfer in a scheme of amalgamation of a capital asset by the amalgamating company to the amalgamated company if the amalgamated company is an Indian company.

(*via*) Any transfer in a scheme of amalgamation, of a capital asset being a share or shares held in an Indian Company, by the amalgamating foreign company to the amalgamated foreign company provided:

(*i*) at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and

(*ii*) such transfer does not attract tax on capital gains in the country in which amalgamating company is incorporated.

This amendment has come into effect from assessment year 1993-94.

(*vii*) Any transfer by a shareholder in a scheme of amalgamation of share or shares held by him in the amalgamating company, if

(*a*) The transfer is made in consideration of the allotment to him of any share or shares in the amalgamating company, and

(*b*) The amalgamated company is an Indian company.

(*viia*) With effect from 1.6.92 the following new sub-section has been inserted by the Finance Act 1992:

any transfer of a capital asset being bonds or shares referred to in 115 AC(1) (units purchased in foreign currency) shall not be regarded as transfer, if such transfer is made outside India by a non-resident to another non-resident.

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(*viii*) Any transfer of agricultural land in India affected before 1st of March 1970.

(*ix*) With effect from 1.4.1977, any transfer of a capital asset, being any work of art, archaeological, scientific or art collection, book, manuscript drawing, painting, photograph or print to the Government, or a university, or the National Museum, National Art Gallery, National Archives or any such other public museum, or institution as may be notified by the Central Government in Official Gazette to be of national importance or to be of renown throughout any State or States.

(*x*) Any transfer by way of conversion of *bonds* debentures, debenture stock or deposit certificates in any form, of a company into shares or debentures of that company.

This point has been inserted by the Finance (No. 2) Act 1991 with retrospective effect from 1.4.1962.

With effect from assessment year 1998-99 following are being inserted :

(*xi*) Any transfer made on or before the 31st day of December 1997 by a person (not being a company) of a capital asset being membership of a stock exchange of a recognised stock exchange to a company in exchange of shares allotted by that company to the transferar.

Explanation. For the purposes of this clause, the expression "membership of a recognised stock exchange" means the membership of a stock exchange in India which is recognised under the provisions of the Securities Contract (Regulation) Act 1956 (42 of 1956).

(*xii*) Any transfer of a capital asset, being land of a sick industrial company, under a scheme prepared and sanctioned under section 18 of the Sick Industrial Companies (Special Provisions) Act 1985 (1 of 1986) where such industrial company is being managed by its workers' co-operative :

Provided that such transfer is made during the period commencing from the previous year in which such has become a sick industrial company and ending with the previous year in which the entire networth of such company becomes equal to or exceeds the accumulated losses.

Distribution of assets by a company in liquidation. Under section 46(1) if a company distributes its assets among its shareholders on account of its liquidation, such distributions shall not be regarded as transfer in the hands of the company. u/s 46(2) if a shareholder receives any money or assets from the company, he shall be liable to tax on the excess of fair market value or sale proceeds (if sold) of such assets on the date of distribution over the cost of acquisition of shares held by assessee and such an amount which is assessable under the dividend clause, *e.g.*, if a person receives some assets from a company in liquidation whose fair market value is Rs. 50,000. The assessee held 300 shares which he had purchased for Rs. 125 each. The value of assets distributed included a sum of Rs. 10,000 taxable as dividend. In this case the capital gain shall be:

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	F.M.V.		Rs. 50,000
	Cost of acquisition of—		
(*a*)	300 shares @ Rs. 125 each	= 37,500	
(*b*)	Amount taxable as dividend	= 10,000	
			47,500
	Capital Gain		2,500

Deemed Capital Gain [Section 47A]

In case an asset is transferred from a parent company to a subsidiary company or from subsidiary company to a parent company [Section 47 (*iv*) or (*v*)] and

(*a*) Such capital asset is converted by the transferee company into or is treated by it as stock-in-trade before the expiry of a period of 8 years from the date of transfer, or

(*b*) The parent company or its nominees cease to hold the 100% of share capital of subsidiary company before the expiry of a period of 8 years from the date of transfer, the capital gain which was exempted u/s 47 will become taxable as deemed capital gain of the year in which such transfer took place.

With effect from assessment year 1998-99 the transferor which has transferred its membership of a recognised stock exchange and has received shares as consideration, such shares cannot be transferred for a period of three years from the date of transfer of membership, the amount of exemption claimed under section 47 shall be deemed as income chargeable to tax under the head capital gains.

New Method of Computing Capital Gain [Section 48]

The Finance Act 1992 has changed the method of computation of capital gain. With effect from assessment year 1993-94, the new method of computation of capital gain is as follows:

1. For all assessees and all assets except shares and debentures owned by a non-resident

(*a*) Short-term capital gain shall be computed by deducting out of full value of consideration the following amounts—

(*i*) expenditure incurred wholly and exclusively in connection with such transfer;

(*ii*) the cost of acquisition of the asset; and

(*iii*) the cost of any improvement thereto.

(*b*) Long-term capital gain shall be computed by deducting out of full value of consideration the following amounts—

(*i*) expenditure incurred wholly and exclusively in connection with such transfer;

(*ii*) the indexed cost of acquisition; and

(*iii*) the indexed cost of any improvement thereto.

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For the above purposes—

A. 'Indexed cost of acquisition' means an amount which bears to the cost of acquisition the same proportion as Cost Inflation Index for the first year in which asset was held by the assessee or for the year beginning on the 1st day of April 1981, whichever is later.

B. "Indexed cost of any improvement" means the amount which bears the cost of improvement the same proportion as cost Inflation Index for the year in which the asset is sold bears to the cost Inflation Index for the year in which improvement to the asset took place.

C. "Cost Inflation Index" (C.I.I) for any year means such Index as the Central Government may, having regard to 75% of average rise in the Consumer Price Index for urban non-manual employees for that year, by notification in the Official Gazette, specify in this behalf.

Vide notification No. 9064 Dated 5.8.1992 u/s 48 the Central Govt. has notified the following Cost Inflation Index (C.I.I.) :

Sr. No.	*Financial Year*	*Cost Inflation Index (C.I.I.)*
1	1981—82	100
2	1982—83	109
3	1983—84	116
4	1984—85	125
5	1985—86	133
6	1986—87	140
7	1987—88	150
8	1988—89	161
9	1989—90	172
10	1990—91	182
11	1991—92	199
12	1992—93	223
13	1993—94	244
14	1994—95	259
15	1995—96	281
16	1996—97	305

With effect from assessment year 1998-99 the provisions of Indexing u/s 48 will not be applicable on transfer of long term capital gain arising from transfer of long term bonds or debentures.

INDEXING AT A GLANCE

U/S 48 (iii)

Situation	*Indexing*
1. Short Term Capital assets	No indexing
2. Repurchase of units acquired u/s 80 CCB	No indexing

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3. Bonds and Debentures	No indexing with effect from assessment year 1998-99
4A Long term capital assets acquired before 1.4.81 under gift, will, partition H.U.F. inheritance *i.e.* u/s 49(1)	Actual cost or FMV on 1.4.81 (whichever is more) × CII of the year of sale/CII of 1981-82 *i.e.* 100
4B Cost of improvement incurred after 1.4.81 on above mentioned assets.	Cost of improvement × CII of the year of sale / CII of the year of improvement.
5. Long term capital assets acquired on or after 1.4.1981 (not under any of the modes mentioned in 4 above) Cost of improvement incurred after 1.4.1981 =	Actual cost × CII of the year of sale / CII of the year of acquistion Cost of improvement × CII of the year of sale / CII of the year of improvement
6. Long term capital asset acquired by present seller under section 49(1) after 1.4.81 but was acquired by previous owner before 1.4.81.	Actual cost or FMV on 1.4.81 (whichever is more) × CII of the year of sale/CII of the year in which present seller became its owner

C.I.I. = Cost Inflation Index.

Illustration 1. Cost of acquisition in 1982-83 Rs. 1,20,000. Find out the indexed cost if sold in 1996-97. [C.I.I. for 1982-83 is 109 and for 96-97 is 305.]

Solution

Computation of Indexed cost :—

Cost in 1982-83 = Rs. 1,20,000

Indexed cost = Rs. 1,20,000 × 305/109

= Rs. 3,35,780

Q. No. 1

Shares purchased during 84-85 for Rs. 1,60,000 were sold during 1996-97. Compute the indexed cost of these shares if C.I.I. for 1984-85 was 125 and for 1996-97 it is 305.

[**Hints** : Rs. 3,90,400]

2. For non-resident assessees selling shares or debentures

In case of non-residents, capital gain from shares or debentures shall be computed by converting—

(*i*) the cost of acquisition;

(*ii*) the cost of improvement;

(*iii*) the expenses incurred on sale of such assets; and

(*iv*) the full value of consideration received or accruing;

into the same foreign currency in which such shares or debentures were acquired; and the capital gain so computed in such foreign currency shall be converted into Indian currency. Such method of computation of capital gain shall be applicable in

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respect of capital gains accruing or arising from every reinvestment thereafter in, and sale of, shares or debentures of an Indian Company.

The conversion of Indian currency into foreign currency and reconversion of foreign currency into Indian currency shall be at the rates prescribed in this behalf.

Illustration 2. Find out the inflated cost in following cases (separately for each case) :

(*a*) cost of plot acquired in 1986-87 for Rs. 80,000

(*b*) cost of house purchased in 1979-80 for Rs. 90,000. Fair market value on 1.4.81 being Rs. 1,50,000

(*c*) cost of house purchased in 1976-77 for Rs. 2,00,000. Cost of improvement in 79-80 Rs. 50,000. Fair market value on 1.4.81, 4,00,000. Further improved in 1988-89 at a cost of Rs. 1,00,000.

[Cost Inflation Index for 1981-82 = 100, 86-87 = 140, 88-89 = 161 & 1996-97 = 305]

Solution

Case (*a*) Cost in 1986-87 = Rs. 80,000

Indexed cost = 80,000 × 305/140

= Rs. 1,74,286

Case (*b*) Cost in 1979-80 = Rs. 90,000 or F.M.V. on 1.4.81 Rs. 1,50,000

F.M.V. is to be inflated = 1,50,000 × 305/100 = Rs. 4,57,500

Case (*c*) Cost in 1976-77 Rs. 2,00,000

Add cost of improvements in 1979-80—Rs. 50,000

Cost upto 1.4.81	Rs. 2,50,000
or F.M.V. on 1.4.81	Rs. 4,00,000
whichever is higher is cost	Rs. 4,00,000
Inflated cost (4,00,000 × 305/100)	12,20,000
Inflated cost of Improvements (1,00,000 × 305/161)	1,89,441
Total Indexed cost	14,09,441

Q. No. 2

Mr. Rahman purchased a house on 1-11-83 for Rs. 2,00,000 which was improvised in 1990-91 at the cost of Rs. 1,00,000. What will be its indexed cost during 1996-97 if C.I.I. for 1983-84 is 116, in 1990-91 is 182 and for 1996-97 is 305.

[Hints : Indexed Cost = (Rs. 2,00,000 × 305/116 + Rs. 1,00,000 × 305/182) = Rs. 6,93,444]

Determination of Cost of Acquisition

The cost of acquisition means the price which an assessee has paid to purchase, construct or acquire an asset. No problem arises in finding out the cost of acquisition in case of assessee purchasing, constructing or acquiring the asset himself. But in other cases, there are different rules to determine the cost of acquisition. They are:

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1. In case of assets acquired without paying any price [49 (1)]. Where the asset has become the property of the assessee in any of the ways enumerated below, the cost of acquisition shall be deemed to be the cost at which previous owner had acquired the same plus cost of any improvement by the said previous owner and after deducing depreciation allowed by him. These cases are:

(*i*) any division of assets by H.U.F. among its members on its partial or total partition;

(*ii*) assets received under a gift or will;

(*iii*) (*a*) assets received under succession, inheritance or devolution; or

(*b*) any distribution of assets on the dissolution of firm, body of individuals or other association of persons *where such dissolution has taken place before 1.4.1987; or*

(*c*) any distribution of assets on liquidation of a company; or

(*d*) a transfer to a revocable or irrevocable trust; or

(*e*) any such transfer from a parent company to its wholly owned subsidiary Indian Company or *vice versa.*

(*iv*) any transfer of asset by an individual into the common pool of H.U.F.— the cost to H.U.F. will be the cost borne by individual.

2. Shares in amalgamated company [49 (2)]. In case of amalgamation of a company into an Indian company the cost of acquisition of shares of amalgamated company shall be taken to be the cost of acquisition to him of the shares of the amalgamating company.

3. Cost on conversion of capital assets into trading assets or stock-in-trade. When a capital asset is converted into a trading asset then the cost of the capital asset which is so converted into stock-in-trade of assessee's business may be taken as the market value of those assets on the date of such conversion. In a case *[C.I.T. v. Bai Sirinbai K. Kooka (1982) 46 I.T.R. 80].* Supreme Court held that when the assessee converts his shares into a trading asset of his business on becoming a dealer in shares, the cost of the shares to the business was the market value on the date of conversion.

This decision has been reversed by Taxation Laws (Amendment) Act, 1984 and from assessment year 1985-86, the conversion of capital asset into stock-in-trade is deemed to be transfer and difference between market value and cost is deemed to be capital gain.

4. Cost in case of deemed capital gain u/s 47 A [Section 49 (3)]. Where the capital gain arising from the transfer of a capital asset is deemed to be income chargeable under the head capital gains as a result of operation of provisions of section 47A, the cost of acquisition of such asset to the transferee company shall be the cost for which such asset was acquired by it.

5. Assets on which depreciation has been claimed [Section 50]. In case assets are sold during the previous year and some gain occurs, this capital gain is taxable under this head. Section 50 of the Income-tax Act provides the procedure for calculation of deemed capital gain/loss in case of depreciable assets. This section provides for two different situations:

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1. *Transfer of one or more assets in the block of assets [Section 50(1)]*

Where the full value of the consideration received or accruing due to transfer of one or more assets belonging to same block of assets exceeds the aggregate of the following amounts:

(*i*) expenditure incurred in connection with such transfer;

(*ii*) the W.D.V. of such block of assets at the beginning of previous year; and

(*iii*) the actual cost of any asset falling within that block of assets acquired during the year.

Such excess shall be deemed to be the short-term capital gain.

2. *Transfer of all the assets within same block of assets and the block ceases to exist. [Section 50(2)]*

In such event the written down value of such block plus cost of any new asset acquired during the year is taken as actual cost if it is less than total consideration received, the income, if any, as a result of such transfer or transfers shall be deemed to be short-term capital gain.

In case the W.D.V. of the block of assets and cost of new asset acquired during the year added together is more than the total consideration received, the difference is called as short-term capital loss.

6. Advance money received (Section 51). Where the capital asset was, on a previous occasion, the subject of negotiation of the sale etc. any advance or other money received and retained by the assessee in respect of such negotiation, shall be deducted in computing the actual cost of such asset to him.

In case advance money was received by a previous owner and was forefeited, it is not to be reduced out of the cost for calculating capital gain in the hands of present seller.

Illustration 3. Mr. Ghosh sold a house on 1.9.96 for Rs. 6,00,000. This house was inherited by him during 1981-82 from his father who had constructed it in 1971-72 for Rs. 50,000. Mr. Ghosh spent Rs. 50,000 on renovation of the house in 1986-87. Fair market value of the house as on 1-4-1981 was Rs. 1,50,000.

This house was under negotiations for sale in May, 1990 and he received Rs. 80,000 as advance money. The contract could not materialise and the advance money was forfeited. Compute the amount of capital gain assuming that he does not qualify for any exemption.

[C.I.I. for 1981-82 : 100, 86-87 : 140, 90-91 : 182 & 96-97 : 305]

Solution. *Computation of Capital Gain Assessment year 1996-97*

	Rs.	Rs.
Sale Price on 1.9.96		6,00,000
Less: Cost of acquisition	1,50,000	
Less: Advance money forefieted	80,000	
	70,000	
Indexed cost [70,000 × 305/100]	2,13,500	
Indexed cost of improvement [50,000 × 305/140]	1,08,929	3,22,429
Long Term Capital Gain		2,77,571

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7. Cost of acquisition of goodwill [Section 55 (2) (a)]. In case goodwill was purchased, the cost shall be the price paid but in case it was not purchased the cost is taken as NIL.

The Finance Act 1994 has amended the above provision in following manner :

(*a*) In case the capital asset is goodwill, tenancy rights, stage carriage permits or loom hours the cost of acquisition will be—

(*i*) purchase price, if such asset was purchased ; and

(*ii*) NIL in all other cases except those covered u/s 49 (1) (1) to (*iv*).

(*aa*) In case a person is holding shares or other securities and assessee becomes entitled to subscribe to an additional financial asset, the cost of such additional asset shall be :

(*i*) Cost of original asset shall be its purchase price paid.

(*ii*) Incase such right to subscribe is renounced in favour of some other person, the cost of such renounced right is taken as NIL.

(*iii*) In case assessee subscribes to such additional asset, the amount actually paid shall be its cost.

(*iv*) In case asset is acquired by renouncee the cost shall be price paid by him to renouncee and amount paid to the company or institution for such renounced asset.

With effect from assessment year 1998-99 the above mentioned provisions relating to cost of goodwill are being made applicable to a *right to manufacture, produce or process any article or thing.*

8. Adoption of Fair Market Value [Section 55 (2) (*b*) and (*c*)]

(*i*) Where the asset became the property of the assessee before 1st April 1981, it will mean the cost of acquisition of the asset to the assessee or the fair market value of the asset on 1st April 1981, at the option of the assessee.

(*ii*) Where the capital asset becomes the property of the assessee under any of the modes given in section 49, the assessee is given the option to adopt, instead of the cost of the asset to the previous owner or its fair market value as on 1.4.1981.

9. Cost of acquisition of shares [Section 55 (2) (v)]. When an assessee acquires capital asset in the form of shares or stock of a company on:

(*a*) Consolidation and division of the share capital of the company into shares of large denomination than its existing shares.

(*b*) Conversion of any shares into stock,

(*c*) Re-conversion of any stock into shares,

(*d*) Sub-division of any of the shares of the company into shares of smaller amount, or

(*e*) Conversion of one kind of shares into another kind.

The cost of acquisition if these cases means the cost of acquisition of the asset calculated with reference to the cost of acquisition of the shares or stock from which such asset has been derived.

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10. When cost cannot be ascertained [Section 55 (3)].

Where the cost of particular asset, for which the previous owner had acquired the asset, cannot be ascertained, the cost of acquisition to the owner means the fair market value of the asset on the date on which it becomes the property of such owner.

11. Cost of Bonus Shares Act. The Finance Act 1995 has made a major change in determining the cost of bonus shares to be called "financial asset." As per new amendment the cost of financial assets allotted to the assessee without any payment and on the basis of holding of any other financial asset, shall be taken as NIL. This amendment has come into effect from assessment year 1996-97.

Illustration 4. Assessee A is the investor in shares and held 1,000 shares of Rs. 10 each in a company. On 31st March, 1992 he was allotted 1,000 Bonus Shares of the face value of Rs. 10 each. The cost of acquisition of original shares was Rs. 12 each. During the previous year ending 31st March, 1997 assessee sold 500 shares out of his Bonus Shares @ Rs. 14 per share. Compute the capital gain for the assessment year 1997-98 if cost inflation index for 90-91 is 182 and 96-97 is 305.

Solution

	Rs.
Sale price of 500 shares @ Rs. 14 per share	7,000
Less: Cost of 500 Bonus shares	NIL
L.T. Capital Gain	7,000

Cost of Improvement [Section 55 (1)]

(*a*) In relation to a capital asset being goodwill of a business cost of improvement shall be taken to be nil; and

(*b*) In relation to any other asset—the amount spent by assessee on improving the asset after its acquisition.

The improvement to be so taken into account should be of such capital nature as it does not fall in deductions allowed while computing the income chargeable under the heads:

(*i*) Income from house property, (*ii*) Profits & gains of business or profession, and (*iii*) Income from other sources.

Expenditure incurred in connection with transfer

The cost of stamp and registration fees, brokerage, commission and travelling expenses etc., incurred in connection with transfer to the transferee are allowed to be deducted from the full consideration.

EXEMPTED CAPITAL GAINS

1. Capital gain on transfer of Long-term Residential house property (Section 54). When on the transfer of a house property or land appurtenant thereto being

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taxable under the head 'income from house property' owned by an *Individual* and *H.U.F.* there occurs some capital gain and such capital gain is reinvested in:

(*a*) Purchase of another residential house within one year before or two years after the sale of the house, or

(*b*) Construction of new residential house within three years after the sale of the house.

The amount of capital gain so invested shall be exempted from tax.

If the house so acquired by reinvesting capital gain is sold within a period of three years from the date of its purchase or construction, the previously exempted capital gain will be taxable along with the capital gain on the sale of such house, if any, in the current previous year. In the event of loss on sale of new house, it shall be adjusted out of old exempted capital gain [Section 54].

Illustration 5. Compute the taxable capital gain from particulars given below:

(*i*) Net consideration of a residential house Rs. 11,00,000 (2.6.96) [C.I.I. : 305]

(*ii*) Cost of acquisition of this house Rs. 3,00,000 (1.5.87) [C.I.I. : 150]

(*iii*) New House acquired on 1.9.96 for Rs. 4,00,000.

Solution : *Computation of Capital Gain*

	Rs.
Net consideration	11,00,000
Less: Cost (Indexed 3,00,000 × 305/150)	6,10,000
Long-term capital gain	4,90,000
Less: Exempted u/s 54(1)—cost of New house	4,00,000
Taxable Capital Gain	90,000

(Adapted extract from Circular No. 495—Explanatory notes on the Finance Act 1987 *(F No. 131/29/87 T.P.L. dated 22nd Sept. 1987)]*

Non-utilisation of Long-term Capital Gain before filing of return [Section 54(2)]

With effect from 1.4.88 following new provision has been added:

The amount of the capital gain which is not appropriated by the assessee towards the purchase of the new asset made within one year before the date on which the transfer of the original asset took place, or which is not utilised by him for the purchase or construction of the new asset before the date of furnishing the return of income under section 139 shall be deposited by him before furnishing [such deposit being made in any case not later than the due date applicable in the case of the assessee for furnishing the return of income under sub-section (1) of section 139] in an account in any such bank or institution as may be specified in, and utilised in accordance with any scheme which the Central Government may, be notification in the Official Gazette, frame in this behalf and such return shall be accompanied by proof of such deposit; and, for the purposes of sub-section (1), the amount, if any, already utilised by the assessee for the purchase or construction of the new asset together with the amount so deposited shall be deemed to be the cost of the new asset.

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If the amount deposited under this sub-section is not utilised wholly or partly for the purchase or construction of the new asset within the period specified in sub-section (1), then—

(*i*) the amount not so utilised shall be charged under section 45 as the income of the previous year in which period of three years from the date of the transfer of the original asset expires; and

(*ii*) the assessee shall be entitled to withdraw such amount in accordance with the scheme aforesaid.

The effect of this change is that is case assessee is unable to utilise the amount before filing the return of income, he must deposit the unutilised amount in authorised Bank and it can be withdrawn for utilisation in accordance with the scheme notified by Govt. In case amount of deposit is not utilised within prescribed time, it shall be deemed as capital gain of the previous year in which such prescribed time ends.

Q. No. 3

Mr. Vasudev purchased a house in Udipi in 1976 for Rs. 1,00,000. He incurred the following expenses for the improvement of the house.

Renovation of the house Rs. 25,000 and additions of 2 rooms after one year. The F.M.V. of the house on 1.4.81 was Rs. 1,80,000. He sold the house in May 1996 for Rs. 8,50,000.

He purchased another house property within 2 months for Rs. 3,00,000 and invested in Capital Gains Account Scheme Rs. 50,000. Calculate taxable capital gain for the previous year 1996-97. Cost Inflation Index for 1981-82 was 100 for 1996-97 is 305.

[**Hints** : F.M.V. on 1-4-81 as Cost Rs. 1,80,000 Indexed Rs. 1,80,000 × 305/100 = Rs. 5,49,000 LTC Gain Rs. 3,01,000 less exemption u/s 54 Rs. 3,00,000; u/s 54 (2) not allowed Taxable L.T. Capital Gain Rs. 1,000.]

2. Capital Gain on Transfer of Self-cultivated Agricultural Land [Section 54 B]. When on the transfer of agricultural land, which was being used for agricultural purpose by the assessee or his parents for a period of at least two years immediately preceding the year of a transfer and there occurs some capital gain and such capital gain is reinvested in the purchase of agricultural land within a period of 2 years from the date of such transfer, the amount of capital gain so invested shall be exempted from tax.

If the land, so purchased by reinvesting the capital gain, is transferred within a period of 3 years from the date of its purchase, the previously exempted capital gain will be taxable along with the new capital gain on the sale of such land, if any, in the current previous year.

Non-utilisation of Capital Gain before filing of return [Section 54B (2)]

The amount of the capital gain which is not utilised by the assessee for the purchase of the new assets from the date of furnishing the return of income under section 139, shall be deposited by him before furnishing such return [such deposit being made in any case not later than the due date applicable in the case of the assessee for furnishing the return of income under sub-section (1) of section 139] in

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an account in any such bank or institution as may be specified in, and utilised in accordance with, any scheme which the Central Government may, by notification in the Official Gazette, frame in this behalf and such return shall be accompanied by proof of such deposit; and, for the purposes of sub-section (1), the amount, if any, already utilised by the assessee for the purchase of the new asset together with the amount so deposited shall be deemed to be the cost of the new asset:

If the amount deposited under this sub-section is not utilised wholly or partly for the purchase of the asset within the period specified in sub-section (1), then—

(*i*) the amount not so utilised shall be charged under section 48 as the income of the previous year in which the period of two years from the date of the transfer of the original asset expires; and

(*ii*) the assessee shall be entitled to withdraw such amount in accordance with the scheme aforesaid.

$$\text{Deemed LT.C.G} = \text{Exemption u/s 54B(2)} \times \frac{\text{Amount unutilised}}{\text{Amount deposited}}$$

3. Capital Gains on Compulsory Acquisition of Land and Buildings [Section 54 D]. Where the capital gain arises from the transfer by way of compulsory acquisition under any law, if a capital asset being land or building or any right in land or building forming part of an industrial undertaking, which was being used by assessee for two year preceding the previous year in which the asset was acquired for his own business and the assessee reinvests the capital gains from such a transfer in purchase of another land or building or right in land or building or constructs another building within 3 years after the transfer, the capital gain so invested is exempted from tax. If the amount invested is less than the capital gain earned, the balance shall be taxable.

The new asset so purchased cannot be sold or transferred within a period of 3 years from the date of transfer. If sold or transferred earlier, old exempted gain along with new capital gain will be taxable in the previous year in which new asset is transferred.

It can be summarised as follows:

1. Land and building or any right in land and building compulsorily acquired under any law forming part of an industrial undertaking belonging to the assessee.

2. Such land and building must have been used by the assessee for the purposes of the business of the said undertaking during the period of two years immediately preceding the date on which transferred or compulsory acquisition took place.

3. The assessee must have constructed a building or purchased another piece of land by investing capital gain arising on the transfer of the asset within a period of 3 years from the date of such transfer.

4. The land and building acquired by re-investing capital gain must be for the purposes of shifting or re-establishing the said undertaking or setting up another industrial undertaking.

Non-utilisation of Long Term Capital Gain before filing return [Section 54 D(2)]

"The amount of the capital gain which is not utilised by the assessee for the purchase or construction of the new asset before the date of furnishing the return of

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income under Section 139, shall be deposited by him before furnishing such return [such deposit being made in any case not later than the due date applicable in the case of the assessee for furnishing the return of income under sub-section (1) of section [139] in any account in any such bank or institution as may be specified in, and utilised in accordance with, any scheme which the Central Government may by notification in the Official Gazette, frame in this behalf and such return shall be accompanied by proof of such deposit; and, for the purposes of sub-section (1), the amount, if any, already utilised by the assessee for the purchase or construction of the new asset together with the amount so deposited shall be deemed to be the cost of the new asset:

If amount deposited under this sub-section is not utilised wholly or partly for the purchase or construction of the new asset within the period specified in sub-section (1), then—

(*i*) the amount not so utilised shall be charged under section 45 as the income of the previous year in which the period of three years from the date of the transfer of the original asset expires; and

(*ii*) the assessee shall be entitled to withdraw such amount in accordance with the scheme aforesaid.

$$\text{Deemed L.T.C.G.} = \text{Exemption u/s 54 D(2)} \times \frac{\text{Amount unutilised}}{\text{Amount deposited}}$$

4. Exemption in case long term capital gain is invested in specified bonds, debentures or shares of a public company (Section 54EA).

1. In case net consideration, of any or all long term capital assets, transferred during the previous year, is reinvested in bonds, debentures, shares of a public limited company or units of mutual funds [set up u/s 10 (23D)], which are so notified in Official Gazette, within *6 months* from date of transfer of capital asset, the capital gain shall be exempted in following manner :
   (*a*) If whole or more than net consideration of long term capital assets transferred during the previous year is reinvested.....whole of long term capital gain from such assets shall be exempted.
   (*b*) In case amount invested is less than the whole amount of net consideration proportionate amount (to be calculated in following manner) shall be exempted.

$$\text{Exemption u/s 54EA} = \text{Amount of long term capital gains} \times \frac{\text{Amount Invested}}{\text{Amount of Net Consideration}}$$

2. The bonds, debentures shares or units so acquired cannot be sold or otherwise converted into money (cannot be pledged to take loan etc.) for three years from the date of their acquisition. The amount of capital gain which was exempted u/s 54EA shall be deemed as long term capital gain of the year in which such new assets are transferred.
3. The bonds, debentures, shares or units on which benefit u/s 54EA has been claimed, shall not qualify for rebate u/s 88.
4. *Net consideration* means total sale price less expenses on sale, if any.

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5. Exemption in case long term capital gain is invested in specified assets [Section 54EB].

1. In case net consideration, of any or all long term capital assets, transferred during the previous year, is reinvested in any of the assets specified by the Board, which are so notified in Official Gazette, within *6 months* from date of transfer of capital asset, the capital gian shall be exempted in following manner :
   - (*a*) If whole or more than net consideration of long term capital assets transferred during the previous year is reinvested...whole of long term capital gain from such assets shall be exempted.
   - (*b*) In case amount invested is less than the whole amount of net consideration proportionate amount (to be calculated in following manner) shall be exempted.

     Exemption u/s 54EB=Amount of long term capital gain × Amount Invested/Amount of net consideration.
2. The assets so acquired cannot be sold or otherwise converted into money (cannot be pledged to take loan etc.) for *seven years* from the date of their acquisition, the amount of capital gain which was exempted u/s 54EB shall be deemed as long term capital gain of the year in which such new assets are transferred.
3. The assets on which benefit u/s 54EB has been claimed, these shall not qualify for rebate u/s 88.
4. *Net consideration* means total sale price less expenses on sale, if any.

6. Exemption of capital gain on transfer of long-term captial assets in case of investment in residential houses [Section 54F]. In case an individual and HUF transfer any *long-term capitdl asset* (other than the residential house the income of which is taxable under the head 'Income from house property') and constructs a residential house within 3 years after the sale or purchases another residential house within one year before or two years after the sale, so much of capital gain shall be exempted as is in proportion of amount invested to net consideration.

$$\text{Exempted capital gain} = \text{L.T. Capital Gain} \times \frac{\text{Amount invested}}{\text{Net Consideration}}$$

This exemption shall not be allowed if—

(*a*) on the date of transfer assessee owns another residential house; or

(*b*) constructs another residential house within a period of 3 years; or

(*c*) purchases another residential house within a period of two years.

If exemption had been claimed earlier it shall stand forfeited and shall be deemed to be income of that previous year in which new house is acquired or constructed.

Non-utilisation of Net consideration before filing of return [Section 54F (4)]

The amount of the net consideration which is not appropriated by the assessee towards the purchase of the new asset made within one year before the date on which the transfer of the original asset took place, or which is not utilised by him for the purchase or construction of the new asset before the date of furnishing the return of

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income under section 139, shall be deposited by him before furnishing such return [such deposit being made in any case not later than the due date applicable in the case of the assessee for furnishing the return of income under sub-section (1) of section 139] in an account in any such bank or institution as may be specified in, and utilised in accordance with, any scheme which the Central Government may, by notification in the Official Gazette, frame in this behalf and such return shall be accompanied by proof of such deposit, and for purposes of sub-section (1), the amount, if any, already utilised by the assessee for the purchase or construction of the new asset together with amount so deposited shall be deemed to be the cost of the new asset.

If the amount deposited under this sub-section is not utilised wholly or partly for the purchase or construction of the net asset within the period specified in sub-section (1), then—

(*i*) the amount by which—

(*a*) the amount of capital gain arising from the transfer of the original asset not charged under section 45 on the basis of the cost of the new asset as provided in clause (*a*) or, as the case may be, clause (*b*) of sub-section (1) exceeds

(*b*) the amount that would not have been so charged had the amount actually utilised by the assessee for the purchase or construction of the new asset within the period specified in sub-section (1) been the cost of the new asset

shall be charged under section 45 as income of the previous year in which the period of three years from the date of the transfer of the original asset expires; and

(*ii*) the assessee shall be entitled to withdraw the unutilised amount in accordance with the scheme aforesaid.

$$\text{Deemed L.T.C. G} = \text{Exemption u/s 54F (4)} \times \frac{\text{Amount unutilised}}{\text{Amount deposited}}$$

7. Capital Gain on shifting of industrial undertaking from urban areas to non-urban areas [Section 54G]. In case following conditions are fulfilled, the capital gain shall be exempted as per rates given below:

(*i*) Capital asset (P & M, Land, buildings or any right therein) is transferred due to shifting of industrial undertaking from urban areas to rural areas; and

(*ii*) Capital Gain is reinvested within a period of 1 year before or 3 years after the date in:

(*a*) purchase of new machinery or plant for the purposes of business of the industrial undertaking in the area to which the said undertaking is shifted;

(*b*) acquiring building or land or construction of building for the purpose of his business in the said area;

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(*c*) shifting the original asset and transferring the establishment of such undertaking to such area; and

(*d*) incurred expenses on such other purposes as may be specified in a scheme framed by the Central Government for the purposes of this section.

Amount of exemption. In case above-mentioned conditions are fulfilled the amount of exemption under this section will be:

(*i*) if the amount of the capital gain is greater than the cost and expenses incurred in relation to all or any of the purposes mentioned in clauses (a) to (d) (such cost and expenses being hereafter in this section referred to as the new asset), the difference between the amount of the capital gain and the cost of the new asset shall be charged under section 45 as the income of the previous year; and for the purpose of computing in respect of the new asset any capital gain arising from its transfer within a period of three years of its being purchased, acquired, constructed or transferred, as the case may be, the cost shall be nil; or

(*ii*) if the amount of the capital gain is equal to, or less than the cost of the new asset, the capital gain shall not be charged under section 45; and for the purpose of computing in respect of the new asset any capital gain arising from its transfer within a period of three years of its being purchased, acquired, constructed or transferred, as the case may be, the cost shall be reduced by the amount of the capital gain.

Explanation. In this sub-section, "urban area" means any such area within the limits of a municipal corporation or municipality as the Central Government may, having regard to the population, concentration of industries, need for proper planning of the area and other relevant factors, by general or special order, declare to be an urban area for the purposes of this section.

Non-utilisation of amount before filing of return [Section 54G(2)]

The amount of capital gain which is not appropriated by the assessee towards the cost and expenses incurred in relation to all or any of the purposes mentioned in clauses (*a*) to (*d*) of sub-section (1) within one year before the date on which the transfer of the original asset took place, or which is not utilised by him for all or any of the purposes aforesaid before the date of furnishing the return of income under section 139, shall be deposited by him before furnishing such return [such deposit being made in any case not latter than the due applicable in the case of the assessee for furnishing the return of income under sub-section 139] in an account in any such bank or institution as may be specified in, and utilised in accordance with, any scheme which the Central Government may, by notification in the Official Gazette, frame in this behalf and such return shall be accompanied by proof of such deposit; and, for the purposes of sub-section (1), the amount, if any, already utilised by the assessee for all or any of the purposes aforesaid together with the amount so deposited shall be deemed to be the cost of the new asset:

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If the amount deposited under this sub-section is not utilised wholly or partly for all or any of the purposes mentioned in clauses (*a*) to (*d*) of sub-section (1) within the period specified in that sub-section, then—

(*i*) the amount not so utilised shall be charged under section 45 as the income of the previous year in which the period of three years from the date of the transfer of the original asset expires; and

(*ii*) the assessee shall be entitled to withdraw such amount in accordance with the scheme aforesaid.

$$\text{Deemed L.T.C. G} = \text{Exemption u/s 54G (2)} \times \frac{\text{Amount unutilised}}{\text{Amount deposited}}$$

Illustration 6. M/s P. Bros., Ludhiana running an industrial unit were ordered by Municipal Corporation, Ludhiana to shift their concern from urban area of Ludhiana. They shifted their concern during 1996-97 previous year and in this process sold some of the assets whose details are given below:

Asset	*P & M*	*Land*	*Building*
Acquired in	*1987* Rs.	*June 1983* Rs.	*1987* Rs.
Sale Proceeds	10,00,000	6,00,000	12,00,000
W.D.V. on 1.4.96 [cost u/s 50(2)]	4,40,000	—	7,32,500
Cost of acquisition	6,00,000	1,40,000	10,00,000
Amount invested during Dec. '96 due to shifting	8,00,000	2,00,000	5,00,000

Compute the taxable Capital Gain for the assessment year 1997-98 if [C.I.I. for 1983-84 is 116 ; 86-87 : 140, & 1996-97 is 305.]

Solution

Computation of Capital Gain

	P & M Rs.	*Land* Rs.	*Building* Rs.
Sale Proceeds	10,00,000	6,00,000	12,00,000
Less: W.D.V. or Cost (Indexed)	4,40,000	3,68,103	7,32,500
[Land 1,40,000 × 305/116]			
Short-term Capital Gain	5,60,000	2,31,897	4,67,500
Long-term Capital Gain			

Total Capital Gain

		Rs.
S.T. Capital Gain	P & M	5,60,000
	Building	4,67,500
L.T. Capital Gain	Land	2,31,897
		12,59,397

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Less: Exemption u/s 54G—Amount invested in new assets due to shifting:

	Rs.	
P & M	8,00,000	
Land	2,00,000	
Building	5,00,000	
	15,00,000	
As the amount invested is more than the total Capital Gain hence it is fully exempted		12,59,397
Taxable Capital Gain		Nil

8. Investment of compensation received [Section 54H]. In case there is transfer of asset due to compulsory acquisition under any law and the amount of compensation awarded for such acquisition is not received by the assessee on the date of such transfer, the period or period available for depositing or investing the amount under any of the section 54, 54B, 54D, and 54F, in relation to such compensation shall be reckoned from the date of receipt of such compensation.

Where the compensation in respect of original asset by way of compulsory acquisition under any law is received before 1.4.91, and the period for investment has already expired, such period shall stand extended upto 31.12.91.

TREATMENT OF CAPITAL LOSSES

With effect from 1.4.88 *i.e.* assessment year 1988-89 and for capital losses occurring after 1.4.87 the distinction of short-term and long-term has been removed for the purpose of carry forward. In case there is any loss under the head 'Capital Gains' which could not be adjusted during the relevant previous year from the head 'Capital Gains' it can be carried forward for 8 succeeding previous years to be set off only from income under the head "Capital Gains".

Tax on Long term Capital Gains [Section 112]

From assessment year 1993-94 long term capital gain is to be assessed to tax not on normal scheduled rates but on special rates given below :

I. For Individual and H.U.F.

(*a*) Total income shall be reduced by the amount of long term capital gain included in this total income and on balance total income tax is calculated at scheduled rates; and

(*b*) on long term capital gain tax is to be calculated at the rate of 20% of such long term capital gain. In case of firm assessed as firm (PFAF) and firm assessed as AOP (PFAOP) rate of tax on long term capital gain is 20%.

II. For Companies

(*a*) Total income shall be reduced by the amount of long term capital gain if included in total income and on balance total income tax is calculated at scheduled rates; and

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(*b*) on long term capital gain tax is to be calculated at the rate of 30% of such long term capital gain (for venture companies this rate is 30%).

III. Adjustments

1. For allowing deductions u/s 80 Gross Total Income shall be reduced by long term capital gain and balance amount shall be deemed as Gross Total Income for this chapter.

2. Rebate of tax u/s 88 shall be allowed only out of tax on *balance total income i.e.* after deducting long term capital gain.

3. In case of Individuals and H.U.F. if *balance total income* is less than exempted limit, the long term capital gain shall be reduced by such amount by which the total income falls short of exempted limit and on balance long term capital gain tax shall be calculated.

CHART SHOWING THE COMPUTING OF CAPITAL GAINS

Item	*Treatment*
Scope of Charge	*Gain on Transfer of a Capital Asset* called Capital gain, (Section 45).
1. **Capital assets [Section 2(14)]**	Property of any kind held by assessee, whether or not connected with his business of profession. It includes Plant and Machinery. 'Building'—Whether business premises or residential, all assets of a business, goodwill, patent rights, etc.: *does not include* (*i*) Stock in trade, (*ii*) Personal effects—Household goods except Jewellery; (*iii*) Agricultural land situated in rural areas; (*iv*) Gold Bonds 1977 or Gold Bonds 1980; and (*v*) Special Bearer Bonds.
2. **Transfer [Section 2(47)]**	Includes sale, exchange, relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition under any law. It must be effected during the previous year. *Transfer not regarded as transfer* (Section 43) (*i*) Transfer of assets on partition of H.U.F.; (*ii*) Transfer of assets on liquidation of company to its shareholders; (*iii*) Transfer of assets under a gift, will or irrevocable trust; (*iv*) Transfer of assets by a parent company to subsidiary company; (*v*) Transfer of assets by a subsidiary to a parent company provided in (*iv*) and (*v*) the recipient company is Indian Company and parent company holds 100% of share capital of subsidiary company; (*vi*) Transfer of assets on amalgamation of companies; (*vii*) Transfer of shares on amalgamation of companies; (*viii*) Transfer of agricultural land before 1st March 1970; and (*ix*) Transfer of assets of historical importance to a Museum, Archieves or National Gallery of Art. (*x*) Conversion of Bonds and debentures into shares or debentures.

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3. Gain

Capital Gain = Sale Price—
(Section 48)

(*i*) Cost of acquisition [Indexed]
(*ii*) Cost of any improvement [Indexed]
+
(*iii*) Expenses on Transfer
Balance is called Capital Gain.

Cost of acquisition. The cost at which asset was acquired by the assessee. But in following cases, the cost will mean as mentioned against each:

(*a*) *Assets acquired without paying any price*—In case asset is received by way of transfer, under partition of H.U.F., under gift of will, under succession or inheritance on dissolution of firm, on liquidation Company under revocable or irrevocable trust or by a parent company to subsidiary company—the cost will be the cost at which assets were acquired by previous owner plus cost of any improvement less depreciation, if any. [Section 49(1)].

(*b*) *Shares of amalgamated company*—The cost of shares of amalgamated company shall be the cost of acquisition of shares of amalgamating company. [Section 49(2)].

(*c*) *Depreciating assets*—Calculate S.T.C. Gain or Loss as per section 50.

(*d*) *Advance money*—to be adjusted out of cost of acquisition. [Section 51].

(*e*) *Cost is unascertainable*—Fair market value as on the date of acquisition to be taken as cost of acquisition. [Section (56)3].

(*f*) *Option of FMV on 1.4.81.* If an assessee had opted for F.M.V. on 1.4.81, it will be cost of acquisition for all purposes. [Section (55)2].

(*g*) *Cost of Shares*—Cost of new shares received on amalgamation of companies, on transfer of shares into stock or *vice versa* or transfer of lower denomination shares into higher denomination shares or *vice versa;* the cost of acquisition will be the cost at which original shares were acquired. [Section 56(2)(v)].

(*h*) *Cost of Bonus Shares and on renunciation of right shares*—with effect from 1-4-95 it is to be taken as NIL.

Cost of any improvement—An expenditure of capital nature incurred by assessee after acquiring an asset shall be added in cost of acquisition.

Indexing of the Cost of acquisition and cost of improvement of long term capital assets only [Section 48]

Actual Cost and Cost of improvement has to be inflated by using cost inflation Index (C.I.I.) in following manner :—
Indexed cost = Actual cost × C.I.I. of the year of sale/C.I.I of the year of acquisition. Indexed cost of Improvement = Cost of improvement × C.I.I. of the year of sale/C.I.I. of the year of improvement.

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Item	*Treatment*
	No indexing in case of short term capital assets, units acquired u/s 80 CCB and for non resident assessees.
Types of Capital Gain	
1. **Short-term Capital Gain**	Gain on asset held by assessee for a period up to 36 months (In case of shares debentures units securities etc. this period is 12 months).
2. **Long-term Capital Gain**	Gain on asset held by assessee for a period exceeding 36 months (For shares 12 months).
Exempted Capital Gains	
1. **Sale of residential House Property (asset is long-term) [Section 54]**	That part of capital gain of individual and H.U.F. from sale of such house property which is long-term capital asset, is exempted which is invested in— (*i*) purchase of another house within one year before or two years after the sale. (*ii*) construction of another house within 3 years after the sale. *Condition:* Such exempted gain will be added to new capital gain if the new house purchased or constructed is sold or transferred within 3 years from the date of purchase or construction.
2. **Sale of Self-cultivated agricultural land (urban) (Section 54B)**	That part of capital gain from the sale of such land is tax-free which in reinvested in purchase of another piece of land within 2 years after sale.
3. **Compulsory acquisition of Capital assets (Section 54D)**	That part of capital gain arising from compulsory acquisition of land, building or any right is such asset used by assessee for 2 years for his own business, shall be tax-free which is reinvested in purchase of another land or building or right in land or building within 3 years of the acquisition. The new asset so acquired cannot be sold or transferred for a period of 3 years, otherwise old exempted gain will be put to tax.
4. **Exemption in case long term capital gain is invested in specified bonds, debentures or shares of a public company [Section 54 EA]**	1. In case net consideration of any or all long term capital assets transferred during the year is reinvested in bonds, debentures, shares of a public limited co. or units of mutual funds (set up u/s 10 (23D), which are so notified in Official Gazette, within **6 months** from date of transfer of capital asset, the capital gain shall be exempted in following manner :— (*a*) If whole or more than net consideration of long term capital assets transferred during the previous year is reinvested—whole of long term capital gain from such assets shall be exempted. (*b*) In case amount invested is less than the whole amount of net consideration proportionate amount (to be calculated in following manner) shall be exempted. Exemption u/s 54EA = Amount of long term capital gain × Amount Invested/Amount of net consideration 2. The bonds, debentures shares or units so acquired cannot be sold or otherwise converted into money (connot be pledged to take loan etc.) for *three years* from the date of their acquisition, the amount of capital gain which was exempted u/s 54EA shall be deemed as long term capital gain of the year in which such new assets were transferred.

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3. The bonds, debentures, shares or units on which benefit u/s 54 EA has been claimed, shall not qualify for rebate u/s 88.
4. *Net consideration* means total sale price less expenses on sale if any.

5. Exemption in case long term captial gain is invested in specified assets [Section 54EB]

1. In case net consideration of any or all long term capital assets transferred during the year is reinvested in any of the assets specified by the Board, which are so notified in Official Gazette, within *6 months* from date the capital gain shall be exempted in following manner :—

(*a*) If whole or more than net consideration of long term capital assets transferred during the previous year is reinvested—whole of long term capital gain from such assets shall be exempted.

(*b*) In case amount invested is less than the whole amount of net consideration proportionate amount (to be calculated in following manner) shall be exempted. Exemption u/s 54EB = Amount of long term capital gain × Amount Invested/Amount of net consideration

2. The assets so acquired cannot be sold or otherwise converted into money (cannot be pledged to take loan etc.) for seven years from the date of their acquisition, the amount of capital gain which was exempted u/s 54EB shall be deemed as long term capital gain of the year in which such new assets are transferred.

3. The assets on which benefit u/s 54EB has been claimed, these shall not qualify for rebate u/s 88.

4. *Net consideration* means total sale price less expenses on sale if any.

6. Sale of long-term capital assets (Section 54F)

Where a long-term asset is transferred and sale price is reinvested in construction or purchase of a residential within three years or one year before or two years after sale, respectively, so much of capital gain shall be exempted as is in proportion of amount invested to net consideration. No exemption if assessee owns another house or acquires another house in one year before or two years after or constructs another house in three years.

7. Transfer of assets due to shifting of factory from urban to non-urban areas (Section 54G)

In case assessee has to transfer his assets due to shifting of his factory from urban areas to non-urban areas and he purchases new machinery or plan, or acquires land or building or has incurred the expenses on shifting within one year before or two years after sale, the capital gain shall be treated as below:

(*a*) difference between Capital Gain and cost of new asset is taxable u/s 45;

(*b*) if capital gain is less than cost of new asset fully exempted (It is subject to conditions).

8. Gain on compulsory acquisition [Section 54H]

In case compensation on compulsory acquisition is not received after the date of transfer the period available for investment shall be counted from the date of receipt of such compensation.

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Illustration 7. (*i*) Mr. Yash sold an asset on 15.8.96 (C.I.I. 305) for Rs. 64,500. The cost price of the asset purchased on 11.2.76 is Rs. 20,000. The fair market value of the same on 1.4.81 (C.I.I. : 100) was Rs. 20,000. The income of Mr. Yash from other sources during the previous year was Rs. 22,700.

(*ii*) Sh. Dewan, who inherited building properties consisting of a residential house and a shop worth Rs. 1,38,000; sold on 1-11-96 residential property for Rs. 1,56,000 (C.I.I : 305). The fair market value of the property sold was Rs. 50,000 on 1.4.81 (C.I.I. : 100) His income from all other sources was Rs. 12,000.

In the above problem how will the capital gain be treated ?

Solution : *Computation of taxable Capital Gain*	Rs.
(*i*) Sales Price	64,500
Less: F.M.V. on 1.4.81 (Indexed 20,000 × 305/100)	61,000
Capital Gains—Fully taxable	3,500
(*ii*) Sale Price	1,56,000
Less: F.M.V. on 1.4.81 (Indexed 50,000 × 305/100)	1,52,500
Capital Gain—Fully taxable.	3,500

Illustration 8. Mr. James is a film producer. During the previous year he sold a film projector of Rs. 1,70,000 which had cost him Rs. 1,50,000 and in respect of which Rs. 40,000 had been allowed as depreciation during last two years. Besides, his total income from business was Rs. 75,000. Expenses on sale amounts to Rs. 5,000.

Solution : *Computation of Capital Gains*	Rs.
Sale Price of Projector (an item of P & M)	1,70,000
Less: Expenses on sale	5,000
Net Consideration	1,65,000
Less: W.D.V. (1,50,000 – 40,000)	1,10,000
Short-term Capital Gain	55,000

(Under new method of depreciation any amount realised over and above the W.D.V. of asset and cost of transfer is short-term capital gain as block of asset has ceased to exist).

Statement of Total Income

	Rs.
Profits and Gains	
Business Income	75,000
Capital Gains	
Short-Term Capital Gain	55,000
Total Income	1,30,000

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Illustration 9. During the year ended 31st March, 1997 Mr. David sold the following assets:

	Particulars	*Sale Proceeds*
(*i*)	Shop purchased in 1985-86 (C.I.I. 133) for Rs. 18,000	Rs. 45,000
(*ii*)	Machinery purchased in 1983-84 (C.I.I.: 125) for Rs. 50,000 (W.D.V. on 1.4.96 Rs. 35,000)	Rs. 60,000
(*iii*)	Furniture purchased on 1.5.1996 for Rs. 1,000	Rs. 1,300
(*iv*)	Machinery purchased on 1.5.1996 for Rs. 10,000	Rs. 12,000
(*v*)	Agricultural land in Agra purchased in 1979-80 for Rs. 10,000 [F.M.V. on 1.4.81 (C.I.I. : 100) being Rs. 15,000]	Rs. 50,000
(*vi*)	One residential house purchased in 1987-88 (C.I.I. : 150) costing Rs. 30,000	Rs. 63,000

During the year he bought another house for his residence for Rs. 1,50,000.

Work out the amount of Capital Gains to be included in the Gross Total Income and also compute his total income, if his other business income during the year was Rs. 10,000. Cost Inflation Index for 1996-97 is 305.

Solution : *Computation of Capital Gain (Assessment year 1997-98)*

Short-term Capital Gains:	Rs.	Rs.	Rs.
Furniture [being purchased on 1.5.1996] (1,300 – 1,000)]		300	
Machinery: Sale Price (*ii*)	60,000		
Sale Price (*iv*)	12,000		
Total sale price :	72,000		
Less: W.D.V. (10,000 + 35,000)	45,000		
		27,000	
Short-term Capital Gain			27,300
Long-term Capital assets			
(*i*) Residential house : S.P.	63,000		
Less: cost (30,000 × 305/150)	61,000		
Capital Gain	2,000		
Less: exempted u/s 54 : For purchase of new house	2,000		
			NIL
(*ii*) Agricultural land : S.P.	50,000		
Less: F.M.V. on 1.4.81 (15,000 × 305/100)	45,750		
		4,250	
(*iii*) Shop : S.P.	45,000		
Less: cost (18,000 × 305/133)	41,278		
		3,722	

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Total Capital Gain	7,972	
Less: Exempted u/s 54 F—Fully as he has invested Rs. 1,50,000 – 2,000 (exemption u/s 54) = Rs. 1,48,000 in purchase of another house within prescribed period which is more than net consideration of agri. land and shop	7,972	
		Nil
Taxable Capital Gain		27,300

Statement of Total Income

	Rs.	Rs.
Profits and Gains:		
Business Profit		10,000
Capital Gains:		
Short Term Capital Gain	27,300	
Long Term Capital Gain	Nil	
		27,300
G.T.I. being Total Income		37,300

Illustration 10. State whether the following are "Capital assets or not" with reasons for your answer:

(*i*) A car owned by an assessee and used by him and his family.

(*ii*) An air-conditioning plant owned by a company and installed at the residence of its Managing Director.

(*iii*) Silverware belonging to a Hindu Undivided Family which are placed before the family deity (Goddess Lakshmi) at the time of Pooja or worship on special occasions.

Answer

(*i*) A Car owned and used by the assessee for his personal or family purposes falls in the category of personal effects. Had the car been owned by the assessee for his own business, it would have been a capital asset. Any movable asset which is in the nature of personal effects is specially excluded from the definition of capital asset as given in Section 2(14).

(*ii*) An air-conditioning plant owned by the company is a capital asset and it cannot fall in the category of personal effects of the company, company being an artificial person. The use of the plant at the factory premises or the residence of its managing director will not change its nature.

(*iii*) Silverware owned by a H.U.F. and placed before the family deity at the time of Pooja on special occasions is a capital asset of the H.U.F. The ownership of these silverwares continues to be in the H.U.F. and the

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family has not parted with these silverwares as these are placed before the family deity only at the time of Pooja on some special occasions. The Supreme Court has held it to be not a personal effect in a case *Hemant Singhji v. C.I.T. 103 TR 61.*

Q. No. 4

(*a*) Mr. Chandrahas Joshi sold his residential house on 1-11-1996 for Rs. 7,25,000 which he had purchased for Rs. 1,10,000 on 1-2-1982. He spent Rs. 16,100 for its improvement in 1988-89. In 1990-91 he had agreed to sell the house to K. Rajashekar for Rs. 6,50,000 and had received an advance of Rs. 10,000 for the same. However since Mr. Rajashekar did not get the sale registered within the agreed time, the agreement was cancelled and the advance money was forfeited by Mr. Joshi.

Compute the capital gain for the Assessment year 1997-98 assuming that Mr. C. Joshi bought a new residential house in the Previous year 1996-97 for Rs. 2,50,000 and deposited on 1-5-1996 Rs. 1,75,000 in the capital gains account scheme. (The cost inflation index for the financial years 1981-82, 1988-89, 1990-91, and 1996-97 were 100, 161, 182, and 305, respectively). What is the tax payable on the L.T.C.G.? *[Karnataka B.Com. April 1995]*

[**Hints** : Indexed cost (1,10,000 – 10,000) Rs. 3,05,000 + Indexed cost of improvement Rs. 30,500 L.T.C.G 3,89,500 exemption u/s 54 Rs. 2,50,000 exemption u/s 54(2) not allowed] [P-9]

(*b*) From the following information of Mrs. Juhi compute taxable capital gains for the Assessment year 1997-98:

	Rs.
(*i*) Cost of acquisition of residential house in 1983-84	4,64,000
(*ii*) Sale proceeds on 2-8-1996	15,00,000
(*iii*) Cost of construction of new residential house. (The house was constructed during 1996-97. The house is used by Juhi's sister for her residence)	3,00,000

The cost inflation index in 1983-84 was 116 and 1996-97 it is 305.

[**Hints** : L.T.C Gain Rs. 2,80,000 exemption u/s 54 Rs. 2,80,000] [P-9]

(*c*) From the following information relating to previous year 1996-97 compute taxable capital gains of Mrs. Karishma for the Assessment year 1997-98:

	Rs.
(*i*) Purchased agricultural land (Agra city) in 1986-87 (self cultivated)	1,54,000
(*ii*) Sold the land on 10-8-1996 for	6,00,000
(*iii*) Invested in purchase of a house on 10-9-1996 (P.295 Hint)	3,00,000
(*iv*) Purchased another piece of agricultural land on 10-10-1996	1,00,000

The cost inflation index for 1986-87 was 140 and for 1996-97 it was 305. He does not own any other house. *[Karnataka B.Com. 1994]*

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[**Hints :** L.T.C. Gain Rs. 2,64,500 exemption u/s 54B Rs. 1,00,000 exemption u/s 54F Rs. 1,32,250 Taxable L.T.C. Gain Rs. 32,250] [P-9]

Q. No. 5

(*a*) Siddartha converts his plot of land purchased in the year 1981-82 for Rs. 50,000 into-stock-in-trade on 31st March, 1996. The fair market value on 31st March, 1996 is Rs. 1,80,000. The stock-in-trade is sold for Rs. 2,20,000 in the month of January 1997. Find out the taxable income, if any, and so under which 'head of income' and for which assessment year ? The cost of inflation index in 1981-82 was 100, in 1995-96 it was 281 and in 1996-97 it was 305. *[Nagarjuna B.Com. March 1995]*

[**Hints :** Profits and Gains of previous year 1996-97 Rs. 40,000; L.T.C.G. (Deemed Transfer) of previous year 1995-96 = Rs. 39,500] [P-10]

(*b*) Mr. Rama Krishna Raju owned one residential house sold for Rs. 3,40,000 in October 1996 which was actually purchased for Rs. 1,00,000 in 1982-83. He spent Rs. 10,000 for the construction of another room in 1984-85. Expenses incurred in the execution of sale deed were Rs. 10,000 which were borne by him. Cost inflation index Nos. in 1982-83, 1984-85 and 1996-97 were 109, 125 and 305 respectively. Compute his capital gain.

[Nagarjuna B.Com. Sept. 1995]

[**Hints :** Taxable L.T.C. Gain Rs. 25,783] [P-10]

(*c*) Mr. Sundar purchases a house property for Rs. 39,000 on 16.6.70. He gets the first floor of the house constructed in 1972-73 by spending Rs. 60,000. He dies on 12.9.1978. The property transferfed to Mrs. Sundar by his will. Mrs. Sundar spends to Rs. 45,000 during 1984-85 for re-construction of the property. Mrs. Sundar sells the house property for Rs. 16,75,000 on 20th March 1997. Brokerage paid by Mrs. Sundar is Rs. 16,750. The Fair Market value of the house on 1st April 1981 is Rs. 24,000. Compute the capital gain.

Note: 1. Cost inflation index for 1984-85 125, and for 1981-82 is 100.

2. Cost inflation index for 1996-97 is 305.

[Bangalore B.Com. Nov. 1994]

[**Hints :** Cost Rs. 99,000 × 305/100 = 3,01,950 + Indexed cost of improvement Rs. 1,09,800 L.T.C. Gain Rs. 12,46,500] [P-10]

Q. No. 6

(*a*) A joint family purchased a house on 1.5.1985 (C.I.I : 133) in Bombay for Rs. 3.5 lakhs. It sold the house on 10.6.1996 (C.I.I : 305) for Rs. 14 lakhs. On 14.7.1996 it purchased another house at Hardwar at a total cost of Rs. 5 lakhs. It did not own any other house property. Compute the income chargeable under the head "Capital Gains". *[C.A. Inter]*

(*b*) Mr. Nagaraj sold shares of a private sector company on July 10, 1996 (C.I.I : 305) for Rs. 5,05,000 (cost of acquisition on June 15, 1982; (C.I.I : 109) Rs. 60,000, selling expenses amounted to Rs. 5,000. On August 10, 1996 he makes the following investments. Purchase of 3 year National Rural Development Bonds Rs. 1,00,000 and invests

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Rs. 3,50,000 in a resi-dential house at Delhi on July 10, 1996. He does not own any residential House. Determine his Taxable Capital Gain for the Assessment year 1997-98. *[Banglore U., B.Com.]*

[**Hints:** (*a*) Indexed cost 8,02,632 Exemption u/s 54 Rs. 5,00,000; Capital Gain 97,368].

(*b*) Indexed cost 1,67,890 Exemption u/s 54F Rs. 2,32,477 Capital Gain 99,633.] [P-16]

Q. No. 7

(*a*) Mr. X provides the following information regarding his transaction for the sale of residential house during the assessment year 1997-98:

	Rs.
House Purchased in 1978 for	2,50,000
Fair Market Value on 1-4-81 (C.I.I : 100)	4,00,000
Sold in Oct. 1996 (C.I.I : 305)	15,00,000
Amount invested in purchase of another house in April 1996	2,00,000

Compute the amount of taxable Capital Gain.

(Adapted C.A. Inter Nov. 1991)

(*b*) Mr. Z acquired a plot of land on 30.6.86 (C.I.I : 140) for Rs. 2,20,000 and spent Rs. 1,48,500 on its registration and brokerage etc. This plot was sold for Rs. 10 lakhs on 30.6.96 (C.I.I : 305). He had purchased a house for Rs. 4,00,000 on 1.8.95 for his own residence. He had paid Rs. 5,000 as ground rent of plot held by him. Compute the amount of taxable capital gain for the assessment year 1997-98.

(Adapted C.A Inter. May 1992)

[**Hints :** (*a*) LTC Gain 2,80,000; Exemption u/s 54 Rs. 2,00,000; Taxable Capital Gain 80,000 (*b*) Indexed Cost Rs. 8,02,804; LTC Gain Rs. 1,97,196; Exemption u/s 54F Rs. 78,878; Taxable Capital Gain Rs. 1,18,318] [P-17]

Q. No. 8

Prof. Kashinath had purchased shares in a company on 1.3.1984 for Rs. 21,800 and on 1.3.1996 for Rs. 22,300. He sold the shares of 1.3.1984 for Rs. 1,60,000 and of 1.3.1996 for Rs. 80,000 on 1.1.1997. He also sold his jewellery for Rs. 2,00,000 on the same day (1.1.1997) which he had purchased for Rs. 42,000 on 1.8.86.

He invested the full consideration amount from the sale of all these assets in the acquisition of a new residential house on the same day.

Compute taxable capital gain of Prof. Kashinath for the Assessment year 1997-98 assuming that he did not own any residential house on the date of sale of the shares and jewellery. Cost inflation Index for 1983-84, 1986-87, 1994-95 and 1996-97 are 116, 140, 259 and 305 respectively.

[Karnataka B.Com. April 1995]

[**Hints :** Shares L.T.C. Gain Rs. 1,02,681, shares purchased on 1.3.1996 S.T.C. Gain Rs. 57,700; Jewellery L.T.C. Gain Rs. 1,08,500; L.T.C. Gain of shares and jewellery exempted u/s 54F. Taxable S.T.C. Gain Rs. 57,700] [P-14]

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Q. No. 9

From the particulars given by Ramesh, compute the taxable capital gain for the assessment year 1997-98 :

Name of asset	*Date of Purchase*	*Cost Rs.*	*Date of Sale*	*Sale Price Rs.*	*Exp. Rs.*
Govt. Securities	1.10.1995	10,000	30.6.96	15,000	200
Furniture (W.D.V. on 1.4.96 Rs. 4,000)	15.2.91	5,000	20.2.97	3,000	—
Land (Fair Market Value on 1.4.81 Rs. 25,000)	10.1.72	20,000	6.1.97	50,000	1,000
Residential House	1.12.85	60,000	5.5.96	3,00,000	2,000

The assessee has no other residential house on 5.5.96. He purchased another house for residential purposes on 20.3.97 for Rs. 1,30,000. C.I.I. for 1996-97 is 305, 1994-95 259, 1990-91 is 182, and for 1985-86 is 133.

[**Hints :** Govt. securities S.T.C. Gain Rs. 4,800; Furniture S.T.C. Loss Rs. 1,000; Land-Long term capital loss Rs. 27,250; Residential house L.T.C. Gain Rs. 1,60,406 less exemption u/s 54 Rs. 1,30,000 Total Capital Gain Rs. 6,956] [P-13]

Q. No. 10

	Rs.
(*i*) Sale Price of Jewellery in Oct. 1996 (C.I.I : 305)	20,00,000
(*ii*) Cost of acquisition in 1983-84 (C.I.I. : 116)	3,00,000
(*iii*) Amount invested in construction of new house upto 30.6.97	4,00,000
(*iv*) Amount deposited in Capital Gain Deposit Scheme for completing the construction of house (Deposited on 27.6.97)	12,00,000

Compute the taxable capital gain assuming that he does not own any other house. Compute deemed capital gain if he is able to invest Rs. 10,00,000 out of amount deposited in Capital Gain Deposit Scheme ?.

[**Hints :** Indexed Cost Rs. 7,88,793; Exemption u/s 54F Rs. 2,42,241; u/s 54F (4) Rs. 7,26,724; Taxable Capital Gain Rs. 2,42,242 Deemed L.T.C.G. Rs. 1,21,121] [P-18]

Q. No.11

From the following particulars, compute the total income of Sh. Ram Lal for the assessment year 1997-98:

(*i*) Machinery purchased at a cost of in 1981	Rs. 5,00,000
Depreciation allowed from 1.1.1981 to 31.3.1996	Rs. 3,00,000
Sale Price of Machinery on 30.6.1996	Rs. 7,00,000
(*ii*) Sale Price of Commercial Building purchased in 1983-84 (C.I.I : 116) at the cost of Rs. 20,000 and cost of improvements made in 1985-86 (C.I.I : 133) Rs. 20,000	Rs. 1,20,000

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(*iii*) Business Income Rs. 1,00,000

Cost inflation index for 96-97 is 305

[**Hints:** STCG Rs. 5,00,000 L.T.C. asset Indexed cost (52,586 + 45,865) capital gain 21,549 Total Income 6,21,549] [P-19]

Q. No. 12

From the particulars given below compute the taxable income of Sh. A.K. Syal for the assessment year 1997-98:

	Rs.
(*i*) Sale price of shares of A Ltd. acquired on 1.6.1995 and sold on 1.5.96	2,00,000
Cost price of these shares	1,00,000
(*ii*) Sale price of shares of B Ltd. acquired in 1989-90 (C.I.I : 172) sold on 1.12.1996 (C.I.I. 305)	10,000
Cost price of shares of B Ltd.	60,000
(*iii*) Sale price of Jewellery sold on 1.9.96	1,60,000
Cost of Jewellery acquired in 1985-86 (C.I.I : 133)	60,000

Capital loss of Rs. 16,000 has bean B/F from assessment year 1994-95.

[**Hints:** S.T.C. gain Rs. 1,00,000; L.T.C. Gain Jewellery Rs. 22.406; L.T.C. loss shares Rs. 96,395*Less* B/F capital loss Rs. 16,000 Taxable Capital Gain Rs. 10,011] [P-5].

Q. No. 13

An assessee, an individual owns several assets. He sold the following assets during the financial year 96-97 :

(*a*) Shares sold for Rs. 40,000 on 20.12.96. These were purchased in Sept. 94 for Rs. 65,000.

(*b*) Sale of listed Debentures for Rs. 20,000 on 31.1.97. These were purchased in June 93 for Rs. 30,000.

(*c*) Sale of Residential House. It was inherited from his father in June 79. It was built at a cost of Rs. 1,00,000 by his father in 1975. Additions were made by him at a cost of Rs. 50,000 in May 1982. Its Fair Market Value as on 1.4.81 was Rs. 3,00,000. Alterations and Additions were made in March 1990 at a cost of Rs. 80,000. This property was sold for Rs. 17,00,000 in June 96. The selling expenses were Rs. 20,000 on Brokerage etc. He purchased another residential House for Rs. 2,50,000 in Dec. 96 :

Compute taxable capital gain for the Assessment year 1997-98 if C.I.I. for 1981-82 = 100, 1982-83 = 109, 1989-90 = 172, 1993-94 = 244, 1994-95 = 259 and for 1996-97 is 305. *[Bangalore B.Com. Nov. 1993]*

[**Hints :** Shares L.T.C. Loss Rs. 36,544; Debentures L.T.C. Loss Rs. 17,500; Residential house L.T.C. Gain Rs. 4,83,232 less exemption u/s 54 Rs. 2,50,000. Balance L.T.C. Gain Rs. 2,33,232; Capital loss to be adjusted Taxable Capital Gain Rs. 1,79,188] [P-15]

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Q. No. 14

Shri Ram Nath Sukla has given the following information regarding his investments:

(*a*) Shares in Companies:

Name of the Companies	*Date of Purchase*	*C.I.I*	*Cost Price*	*Date of Sale*	*Sale Price*
(*i*) A Ltd.	1.1.85	(125)	7,000	30.6.96	18,000
(*ii*) B Ltd.	1.1.86	(133)	10,000	31.10.96	9,000
(*iii*) C Ltd.	31.1.96	(259)	20,000	30.12.96	26,000
(*iv*) D Ltd.	28.2.96	(259)	18,000	31.1.97	14,000
(*b*) House Properties:					
(*i*) Ownership of flat at Marine Drive (self-occupied)	1.12.87	(150)	90,000	30.6.96	2,00,000
(*ii*) Shop at Poona (let-out)	30.6.86	(140)	50,000	30.9.96	1,20,000

He has purchased a bungalow for his personal residence at Juhu (Bombay) on 31st October 1996 for Rs. 1,60,000. He has incurred an expenditure of Rs. 6,071 on registration and brokerage on the sale of house property in Poona. (C.I.I for 1996-97 is 305).

Compute the net amount of capital gains on which he will have to pay tax for the year ended 31st March, 1997. *[Punjab B.Com., April 1980]*

[**Hints:** S.T.C.G. Rs. 6,000 LTCG Residential house—Fully Exempted u/s 54 LTCG Shares Rs. 920 and shop Rs. 5,000 Fully exempted u/s 54F.

S.T.C. Loss Rs. 4,000 LTC Loss Rs. 13,932 to be C/F Rs. 11,932] [P-1].

Q. No. 15

Mr. Barua, a rich man of Calcutta, has sold the following properties during the year ended on 31st March, 1997 :

(*i*) A house property sold for Rs. 3,40,000 in October, 1996 was actually purchased for Rs. 1,00,000 in 1982-83. He spent Rs. 10,000 for the construction of another room in 1984-85. Expenses incurred in the execution of sale deed were Rs. 10,000 which were borne by him.

(*ii*) On the death of his father in Nov. 1985, few shares were transferred to him which he sold in March 1997 for Rs. 60,000. His father purchased those shares for Rs. 10,000 only in May 1985.

(*iii*) To meet business loss, he had to sell jewellery for Rs. 1,50,000 in October, 1996. The cost of this jewellery is estimated at Rs. 40,000. Jewellery was actually purchased in July 1987 at the time of his marriage.

(*iv*) He also sold an agricultural piece of land at Durgapur in October 1996 for Rs. 90,000 and invested the full sale price within 6 months to buy another agricultural land at Hugli, where he wants to settle now. Land was purchased in October 1994 at a cost of Rs. 30,000 and was cultivated by tenants.

(*v*) He also sold his furniture (Household) for Rs. 10,000. The original cost of furniture Rs. 6,000. The furniture was purchased in 1987 and was sold in December 1996.

Cost Inflation Index for various years is as under :

1982-83	109
1984-85	125
1985-86	133
1987-88	150
1996-97	305

Compute his taxable Capital Gains.

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[**Hints:** Residential house L.T.C.G. Rs. 25,783 shares LTCG Rs. 37,068 Jewellery Rs. 68,667 Agri. land STCG Rs. 60,000 House Hold Furniture Exempted Total Taxable Capital Gain Rs. 1,91,518] [P-3].

Q. No. 16

Mr. Siddaramaiah sold the following assets during the year 1996-97 as he has discontinued his business:

Sale proceeds	Rs.
(*a*) Land purchased in 1981-82 (C.I.I : 100) situated ar Mysore for Rs. 28,000	94,000
(*b*) Machinery purchased for Rs. 12,000 in 1984 (written down value Rs. 6,000)	21,000
(*c*) Office furniture purchased in April 1995 for Rs. 1,200	1,700
(*d*) Shop purchased in 1984-85 (C.I.I : 125) for Rs. 32,000	87,500
(*e*) Residential house purchased in 1981-82 for Rs. 60,000 sold on 15.4.96	2,25,000
(*f*) Rs. 10,000: 10% Debentures purchased on 1.5.1996 sold on 16th March 1997	12,000

(Interest is payable in June and December every year).

He purchased another residential house on 15.3.97 for Rs. 1,34,000 during the year. Compute his taxable income under the head Capital Gains if C.I.I. for 1996-97 is 305.

[**Hints:** S.T.C. Gain on Machinery Rs. 15,000 Furniture Rs. 500 Debentures Rs. 2,000 L.T.C. Gain—House Rs. 42,000 Fully exempted u/s 54. Shop Rs. 9,420 and land Rs. 8,600 Exempted u/s 54 F Rs. 9,134 Total Taxable Capital Gain Rs. 26,386] [P-4].

Q. No. 17

Following are the particulars of assets sold during the previous year 1996-97. Calculate the taxable amount of Capital Gains if C.I.I for 1996-97 is 305.

Assets	*Year of Acquisition*	*C.I.I.*	*Cost of Acquisition*	*F.M.V. as on 1.4.1981*	*Selling Expenses, Brokerage etc.*	*Selling Price*
			Rs.	*Rs.*	*Rs.*	*Rs.*
Shop	1980-81	(100)	20,000	80,000	10,000	2,57,000
Jewellery	1980-81	(100)	10,000	90,000	—	2,90,000
Shares	1982-83	(109)	15,000	—	7,000	70,000
Shares	1990-91	(182)	50,000	—	5,000	30,000
Plant (Depreciable)	1982-83	(109)	4,00,000 (WDV)	—	—	7,00,000
Residential House	1984-85	(125)	70,000	—	—	1,90,000

[**Hints:** STC Gain (Plant) Rs. 3,00,000 LTC Gain House Rs. 19,200 Shop Rs. 3,000 Jewellery Rs. 15,500 Shares Rs. 21,028 Total Capital Gain Rs. 3,58,728 Less L.T.C Loss 58,791 Taxable Capital Gain Rs. 2,99,937] [P-6]

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Q. No. 18

Mr. Pawar had only one house in Bombay which he happens to sell on 10th October, 1996 [C.I.I. for 1996-97 = 305] for Rs. 20,00,000. His expenses are as follows:

	Rs.
Cost of Plot	1,00,000
Date of Purchase of Plot 15.12.83 (C.I.I : 116)	
Cost of Construction in 1984-85 (C.I.I : 125)	2,00,000
Additions made in 1986-87 (C.I.I. : 140)	1,00,000

He makes the following investments:

Purchase of Notified units of U.T.I. on 12th March 1997 for Rs. 4,00,000. Purchase of a shop on the same day for Rs. 2,00,000. Investment of Rs. 1,00,000 was made in notified Government securities on 8th April 1997 Rs. 6,00,000 was deposited in a Nationalised Bank on 20th June 1997 to be utilised for the purchase or construction of a residential house. Assume that—on 20th March 1998 he withdraws the amount from the bank and purchased a residential house in Delhi for Rs. 5,00,000.

Determine the taxable amount of capital gains during the relevant previous years.

[**Hints:** Indexed cost of plot Rs. 2,62,931 Indexed cost of construction Rs. 4,88,000 Indexed cost of addition Rs. 2,17,857 L.T. Capital Gain Rs. 10,31,212 Less exemption u/s 54(2) Rs. 6,00,000 Taxable C. Gain Rs. 4,31,212 *Assessment year 1999-2000* Deemed capital Gain Rs. 1,00,000] [P-8]

Q. No. 19

From particulars given below: Compute the amount of Capital Gain taxable in respective assessment year if C.I.I. for 1985-86 is 133, for 1991-92 is 199 and for 1996-97 is 305 :

		I	*II*
Name of Asset		*Residential House*	*Shares*
Date of Sale		4.1.1997	16.12.96
Date of acquisition		1.4.1985	12.12.91
Sale Proceeds		Rs. 12,00,000	Rs. 6,45,000
Expenses on Sale		Nil	Rs. 5,000
Cost of Asset		Rs. 4,00,000	Rs. 3,00,000
Amount Invested	(*i*)	In construction of New House upto 30.6.97 Rs. 2,00,000	(*i*) In purchase of Bonds of IDBI Rs. 3,20,000 on 31.3.97
	(*ii*)	In purchase of Rural Development Bonds on 31.7.97 Rs. 1,00,000	(*ii*) Nil
	(*iii*)	Amount deposited in Bank under Capital Gains Deposit Scheme on 1.6.97 Rs. 50,000	(*iii*) Nil

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Assume: (*i*) Amount spent by 4.1.2000 *in completion of house* (withdrawn out of amount deposited under Capital Gain Deposit Scheme) is Rs. 30,000

[**Hints:** House Indexed cost Rs. 9,17,293 [L.T.C.G. 2,82,707] Less. Exemption u/s 54 Rs. 2,00,000 u/s 54(2) Rs. 50,000 Capital Gain Rs. 32,707; Shares Indexed cost Rs. 4,59,799 Taxable LTC Gain Rs. 1,80,201 Total C Gain Rs. 2,12,908.] Deemed LTCG of Assessment year 2000-2001 Rs. 20,000 [P-7]

Q. No. 20

Mr. Amol purchased 500 equity shares of Rs. 10 each for Rs. 56 per share in 1983-84. In May 1989 he received 200 bonus shares. On January 13, 1993 he invested in 200 shares @ Rs. 30 each allotted to him as right issue. In December 1996 he sold 200 bonus shares at Rs. 100 each and 100 right shares @ Rs. 50 per share on January 31, 1997. Find out the taxable capital gain if Cost Inflation Index for

1983-84	116
1989-90	172
1992-93	223
1996-97	305

[**Hints :** Cost of Bonus shares NIL L.T.C. Gain Rs. 20,000 cost of right shares [3,000 × 305/223 = 4,103] L.T.C.G. 897] [P-11]

Q. No. 21

X and Y form a partnership firm. Soon after its formation, X brings the following assets as his capital contribution :

	Gold	*Silver*
	Rs.	Rs.
F.M.V. on the date of transfer	5,40,000	72,000
Amount recorded in books	6,00,000	50,000
Actual Cost	30,000	12,000
Year of acquisition	1984-85	1990-91
Cost of Inflation Index for the year of acquisition	125	182
Cost Inflation Index for the year of 1996-97	305	305

Rs. 6,50,000 have been credited in the capital account of X in the firm. Compute the taxable capital gain of X, if any.

[B. Com. Panjab University, April 1994]

[**Hints** : LTCG Gold Rs. 5,26,800 : Silver Rs. 29,890 Total C.G. 5,56,690] [P-12].

Q. No. 22

Mr. B.M. Chatterjee owns many properties in India. He sold some of these during the previous year 1-4-96 to 31-3-1997.

1. Jewellery costing Rs. 80,000 (which was acquired in June 1994 was sold for Rs. 1,00,000 in May, 1996.
2. House at Calcutta : Let-out for residential purposes. It was inherited by him in 1964 : Sale Price on 31-10-96 Rs. 3,80,000. Fair Market value on 1-4-1981 Rs. one lakh. Cost of improvement made during 1989-90 Rs. 25,000. Expenses on transfer are Rs. 25,000.

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3. Household furniture costing Rs. 14,000 in 1987 was sold in March, 97 for Rs. 26,000.
4. Sale price of Padmini car which was purchased by him in Jan. 1990 for Rs. 72,000 was sold on 1-12-96 for Rs. 45,000. Written down value on 1-4-96 was Rs. 38,000.
5. Self-cultivated land was sold for Rs. 2,50,000 on 1-1-97 and its cost in 1982-83 was Rs. 80,000. He purchased a new piece of land for his own cultivation for Rs. 1,50,000 in June 1997.

From the above particulars, compute his total income assuming that he has no other income except these and cost inflation indices are 1981-82 100 ; 19982-83 109 ; 1989-90 172 and 1996-97 305.

[**Hints.** S.T.C. Gain Jewellary Rs. 20,000, Car Rs. 7,000 L.T.C. Gain House Rs. 5,669, Land Rs. 26,147 Fully exempted u/s 54 B. Total capital gain Rs. 32,669] [P-2].

QUESTIONS

1. Define the 'Capital Gain'. Discuss the procedure for computation of Capital Gains as prescribed by the Income-tax Act, 1961.
2. What is the meaning of term, 'Cost of acquisition' as used in the head 'Capital Gains'? What rules are given for the determination of cost of acquisition?
3. Write short notes on: (*i*) Transfer, (*ii*) Capital Gains exempted from Tax, (*iii*) Long Term and Short Term Capital Assets and Gains.
4. How will you distinguish between Capital Gain and Income? Why is it important to make this distinction ? *[B.Com Hons., Delhi]*

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6 INCOME FROM OTHER SOURCES

General incomes u/s 56(1)—Instances of these incomes—Specific incomes u/s 56(2)—Dividends u/s 2(22)—Interest on Securities—Deductions u/s 57—Expenses Expressly disallowed u/s 58—Deemed profits u/s 59—Accounting Methods—Chart—Questions.

Nature of the Head

The fifth and residuary head of income is "Income from Other Sources". Every income which does not specifically fall under any of the preceding four heads shall be included in this head. Section 56 in its sweeping language embraces anything which can be described as income and it is taxable under the act unless expressly exempted. This section operates only when a particular income cannot be included in any other head. Under section 56(1) every kind of income which is included in the total income under this Act and which is not chargeable to tax under any of the first four heads specified in section 14 is chargeable to income-tax under the head "Income from Other Sources".

Under section 56(2), in particular, the following incomes shall be chargeable to income-tax under the head "Income from Other Sources":

(*i*) Dividends.

(*ib*) Any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever. These can be called as casual incomes.

(*ic*) With effect from 1-4-87, *i.e.*, assessment year 1988-89 any sum received by assessee from his employees as contribution to any provident fund or superannuation fund or any fund set up under the provisions of the Employees State Insurance Act, 1948 or any other fund for the welfare of such employees [Section 2(24) (X)] if such income is not chargeable to tax under the head "Profits and Gains of Business or Profession".

(*id*) Any income by way of interest on securities if the income is not chargeable to tax under the head "Profits and Gains of Business or Profession".

(*iv*) Income from machinery, plant and furniture belonging to the assessee and let on hire, if the income is not chargeable to income-tax under the head "Profits and Gains of Business or Profession".

*Malcolm *vs.* Lockhart (1919) 7 Tax Cas 99.

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(v) Where an assessee lets on hire, machinery, plant or furniture belonging to him and also building and the letting of the building is inseparable from the letting of the said machinery, plant or furniture, the income from such letting if it is not chargeable to income-tax under the head "Profits and Gains of Business or Profession."

Under the provisions of section 56(1), the head will operate only when the first four heads of income are exhausted. The onus will be on the assessee to prove that the particular income does not fall under any of the preceding four heads.

Instances of Incomes falling under Section 56(1) (General Incomes)

(i) Income derived by a coal mine owner from rent and royalties are included in this head.

(ii) Income earned by an assessee from licences granted to brick-makers, to erect brickkilns upon his land and to take away the brick-earth and use it for making bricks.

(iii) Remuneration received merely for being a director and not as employees, is not salary but income from other sources.

(iv) Income received by an assessee from a person other than his employer. *e.g.* university remuneration.

(v) Interest on loans, securities, deposits and current account also come under this head. (Interest on co-operative debentures).

Definition of interest u/s (28 A). "Interest" means interest payable in any manner in respect of any money borrowed or debt incurred (including a deposit, claim or other similar right or obligation) and includes any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilised.

(vi) Income received by a professional man as a university examiner.

(vii) Income received on *sub-letting* of the house.

(viii) *Tips* received by a waiter or taxi driver, not being given by his employer.

(ix) Family pension received by legal heirs of employee.

(x) Deemed Incomes.

(xi) Income of other persons to be included in the income of Individual.

(xii) Income from writing articles by a non-journalist.

(xiii) Any withdraw from National Saving Scheme upto an amount on which deduction u/s 80 CCA has been claimed.

(xiv) Income from agricultural land situated outside India.

(xv) Remuneration for lectures delivered outside India.

(xvi) Agency commission received by an agent of life insurance corporation, postal savings, Unit Trust of India or other mutual funds.

Instances of Incomes falling under Section 56(2) (Specific Incomes)

1. Dividend. Incomes from all dividends is specifically included in this head. The shares may be held as stock-in-trade but any dividend received during the period when they are held by the assessee shall be taxable under this head.

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The term dividend has been defined in any inclusive manner under section 2(22). The definition is divided in sub-clauses (*a*) to (*e*) and contains three explanations.

(*i*) *Sub-clause* (*a*)—*Any distribution by a company of accumulated profit entailing release of company's assets.* This provision relates to bonus shares. The two conditions which must be fulfilled for including a particular distribution of profits by a company as dividend are: (*i*) it must be out of accumulated profits, and (*ii*) it must entail the release of the assets of the company.

The issue of bonus shares out of capitalised accumulated profits does not entail the release of any asset and as such the bonus shares are not dividend when they are issued to holders of equity or ordinary shares.

But the position will be entirely different if the company, instead of issuing its own shares, purchases the shares of another company out of its accumulated profits and then issues them to its shareholders. In this case it will amount to release of assets, *i.e.*, shares of another company, and as such the shareholders receiving such shares will have to pay tax on the value of such shares as dividend.

Sometimes company offers two options—either to take bonus share or their cash value. If the shareholders opt for bonus shares they will not be liable to tax but if they opt for cash, the amount will be taxable as dividend.

When the redeemable preference shares are issued as bonus shares out of accumulated profits and they are paid off, the amount so received by an assessee will be taxable as dividend under section 2(22), sub-clause (*a*).

(*ii*) *Sub-clause* (*b*)—*Any distribution, by a company of debentures, stock, deposit certificates and bonus shares to preference shareholders.* Under the provisions of this section, the dividend includes any distribution by a company of debentures, or stock or deposit certificates to the extent to which the company possesses accumulated profit, whether capitalised or not.

Any bonus shares distributed among the preference shareholders will amount to dividend but bonus shares issued to ordinary shareholders are not taxable.

(*iii*) *Sub-clause* (*c*)—*Any distribution made to the shareholders on the liquidation of the company.* Any distribution made by a company to its shareholders on its liquidation to the extent the company possessed accumulated profits before its liquidation shall amount to dividend and will be chargeable to tax under this head. It is immaterial whether such accumulated profits are capitalised or not.

(*iv*) *Sub-clause* (*d*)—*Distribution on reduction of capital.* If, at any time, it is felt that company is over capitalised and has accumulated profits, if the capital of such company is reduced by way of paying its share capital in excess of its needs.

In such cases, any distribution made by a company to its shareholders on reduction of capital to the extent it possesses accumulated profits will amount to dividend and shall be chargeable to tax under this head. It is not necessary to capitalise such accumulated profits.

(*v*) *Sub-clause* (*e*)—*Any payment by a company to its shareholders.* If a company in which public are not substantially interested makes a payment of any of the three kinds mentioned below, to a person who is the beneficial owner of shares (not being the shares entitled to fixed rate of dividend whether with or without a right

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to participate in profits) holding not less than 10% of the voting power or to a concern in which such shareholder is a member or a partner holding a substantial interest such a payment shall be considered as dividend.

The payments may be of any of the following three types:

(*a*) Any payment amounting to any sum.

(*b*) Any payment on behalf of shareholder.

(*c*) Any loan or advance for the individual benefit of a shareholder.

The company must possess accumulated profits to the extent of any such payment. If the payment exceeds accumulated profits the payment limited to the extent of accumulated profits shall be considered as dividend.

Every such payment is taxable as dividend under this head. Such amount shall be put to tax in the year in which such payment is made to or on behalf of shareholder.

Note: Accumulated profits include all profits of the company up to the date of distribution except capital gains arising before 1st April, 1946 or between 1-4-1948 to 31-3-1956.

(*vi*) *Dividend does not include*—(*a*) Referring to sub-clauses (*c*) and (*d*) above if any distribution is made in respect of any shares issued for full cash consideration, where such shareholder is not entitled, in the event of liquidation of company, to participate in the surplus assets.

(*b*) Referring to sub-clauses (*c*) and (*d*), if any distribution is made and such distribution is attribution to the capitalised profits of the company representing bonus shares allotted to its equity shareholders after 31st March, 1964 and before 1st April, 1965.

(*c*) If any payment is made to shareholder under sub-clause (*e*), by a company in ordinary course of its business where the lending of money is the substantial part of the business of the company.

(*d*) Any dividend paid by a company which is set off by the company against the whole or any part of sum previously paid by a company as advance or loan under the provisions of sub-clause (*e*).

Illustration 1. 'B' is a holder of 5,000 equity shares of Rs. 100 each (fully paid) in 'M' & Co. Ltd. On 1-1-1995 the company decided to issue to its equity shareholders bonus shares out of the balance in the General Reserve Account at the rate of one bonus share of Rs. 100 each (fully paid) for every five shares held by them. On 31st March, 1997 'B' received 1,000 bonus shares from the company, the market value of the bonus share on that date being Rs. 120 per share. Discuss 'B's liability to tax in respect of the bonus shares received by him. Would your answer be any different if 'B' had received the bonus shares as a holder of company's preference shares ?

Solution

The issue of bonus shares out of capitalised accumulated profits does not entail the release of any asset and as such bonus shares are not dividend when they are issued to holders of equity and ordinary shares. Two conditions must be fulfilled to include the issue of bonus shares in category of dividend which is taxable in the hands of the recipient shareholder. These conditions are:

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(*a*) Dividend must have been issued out of accumulated profit of the company, and

(*b*) It must entail the release of the assets of the company. Since in the above issue of bonus shares to equity shareholders does not entail the release of the assets of the company, so this does not constitute dividend in the hands of the shareholder.

But bonus shares distributed amongst the preference shareholders will amount to dividend. Mr. B would be chargeable to tax in respect of the market value of the bonus shares at the time of their issue by treating the same as income from dividends.

Q. No. 1

Mr. D holds 2,000 preference shares of Rs. 100 each in a company. Company had reserves worth Rs. 50,00,000. Out of these reserves it issued bonus shares in the ratio of 1 : 4. Market value of these shares amounts to Rs. 116/- per share. How will they be treated in the hands of Mr. D ?

[**Hints :** u/s 2(22) to be treated as dividend—Rs. 58,000]

(*vii*) *Rules regarding taxation of dividends:* (*a*) Dividend is chargeable to tax in the previous year in which it is so declared, distributed, or paid [3(*a*)].

(*b*) Interim dividend is not chargeable to tax in the year in which it is actually declared but is deemed to be the income of previous year in which the amount is unconditionally made available to the shareholder [3(*b*)].

(*c*) Any dividend paid by an Indian company outside India shall be deemed to accrue or arise in India [9(*a*)(*iv*)].

(*d*) The full amount of dividend received by a shareholder is taxable in his hands, even if he might have received such dividends from a tea company whose income is constituted in two parts, *i.e.*, 60% by agriculture and 40% by business.

(*e*) In the event of dividend of several years being declared in later year and paid in lump sum in that year, the dividend shall deemed to be the income of the assessee in the previous year for which they are declared.

(*f*) The principal officer of the company is required to deduct tax at source in certain cases at the prescribed rate, *i.e.*, @ 20% during 1996-97, *i.e.*, for assessment year 1997-98 at the time of payment of dividend and the shareholder gets credit when his tax liability is ascertained.

No tax is deducted at source if

(*a*) dividend is paid by a company in which public are substantially interested;

(*b*) the dividend is paid to an individual;

(*c*) it is paid by account payee cheque; and

(*d*) total amount of dividend payable to individual during the previous year does not exceed Rs. 2,500.

With effect from 1.6.1997 a new proviso is being inserted as a result of which no tax shall be deducted in respect of dividend declared, distributed or paid on or after 1.6.1997.

2. Winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature, whatever [Section 56(2) (*iv*)]. Any prize from lottery or crossword puzzle has also been brought under the purview of Income-tax Act. Similarly, the

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prizes won in horses or any income from gambling or betting are also taxable under this head. These incomes are of casual nature but these are taxable under the Act. U/s 10(3) these incomes are exempt upto a total of Rs. 5,000 (Rs. 2,500 in case of race winnings) in a previous year. Tax is deducted on any lottery prize and on race course winning @ 40% if prize exceeds Rs. 5,000 (Rs. 2,500 in case of race winnings) during the financial year 1996-97.

From assessment year 1987-88, the following incomes are to be taxed at prescribed rates (as given below) and balance of total income is to be taxed at scheduled rates:

(*a*) winning from lotteries;
(*b*) winning from crossword puzzles;
(*c*) winning from races including horse races;
(*d*) winning from card games; and
(*e*) winning from gambling and betting.

Total of these incomes shall be exempted upto Rs. 5,000 (Rs. 2,500 in case of race winnings) in a previous year. Excess will form part of Gross total income. Total income will be divided in two parts:

Part (*a*) Consisting of incomes given above—to be assessed to tax @ 40%.
Part (*b*) Balance of total income which shall be assessed to tax at prescribed rates.

Tax @ 40% shall be deducted at source from winning from lotteries, crossword puzzles and races but gross prize (Net Prize received × 100/60) shall form part of total income. No tax shall be deducted at source if prize is upto Rs. 5,000. (Rs. 2,500 in case of race winnings).

With effect from 1.6.1997, where the winnings from lottery are wholly in kind or partly in cash and partly in kind and cash is not sufficient to meet the liability of tax on such winnings, the person responssible for paying such prize must ensure that tax has been paid in respect of the winnings before such prize is released.

3. **Amount deducted by employer.** Any amount deducted by an employer (not carrying on business or profession) as Income-tax, or E.S.I. Fund contribution or their contribution to provident fund etc. shall be treated as income of the year.

4. **Interest on securities.** The following amounts due to an assessee in the previous year shall be chargeable to income-tax under Interest on Securities :

(*i*) Interest on any security of the Central or State Government.
(*ii*) Interest on debentures or other securities for money issued by or on behalf of a local authority or a company or a corporation established by a Central, State or Provincial Act. [Section 2 (28B)].

What is Interest ?

Interest is the return which a person receives from another person for bearing the risk of parting with the money and losing the income which he would have received on such money had he deposited it in a Bank. It simply means the return received by a creditor who has given his money as debt.

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What is Security ?

A security is a document acknowledging the debt taken by a specific authority from general public. It may be named as a 'Debt' 'Loan,' 'Paper', 'Debenture' or 'Security' or 'Certificate'. It is secured in some manner.

Contents of Security. It contains face value of security, date of maturity, rate of interest, date, place and period of payment of interest etc. These are transferable.

Who can issue a Security ? As per section 18, securities may be issued by following authorities:

(*i*) The Central Government;

(*ii*) A State Government;

(*iii*) A Local Authority;

(*iv*) A Company; or

(*v*) A Statutory Corporation.

Taxability of Interest

(*i*) Interest on securities accrues after a fixed period as mentioned on the face of the security itself. In India, generally, interest accrues after a period of six months. Any interest which accrues to a person during the previous year is added in his gross total income.

(*ii*) Interest is taxable on due basis. It is immaterial whether the assessee has received it or not.

(*iii*) The interest on securities issued by Govt. of India accrues in India even if they are enforced for payment outside India. [*C.I.T. v. Bansi Lal Moti Lal*].

(*iv*) Interest accrues on the name of that person on whose name securities stand on the date of accrual of interest. It is immaterial that he purchased these securities a few days earlier than the date of accrual of interest. He has to include full interest in his gross total income.

(*v*) Interest on securities does not accrue on day-to-day basis. It matures into debt overnight, *i.e.*, the day of accrual of interest.

Deduction of tax at source [Section 193]

Before making payment of interest on securities, it is the duty of the security-issuing authority to deduct tax at source on such interest payable at the 'Rates in force' during that previous year. 'Rates in force' means the rate or rates specified for the purpose of deduction by Finance Act of the year in which deduction is to be made. The tax deducted at source will be deposited in the Government Treasury on behalf of the security-holder. The security-holder's account is credited with the amount and while paying tax on the total income the amount deducted at source will be deducted.

However, in the case of the following securities tax is not deducted at source:

(*i*) Interest payable on $4^1/_4\%$ National Defence Bonds, 1972 where the bonds are held by an individual, not being a non-resident, or

(*ii*) $4^1/_4\%$ National Defence Loan, 1968, or $4^3/_4\%$ National Defence Loan, 1972, provided the interest is payable to an individual, or

(*iii*) Interest payable on National Development Bonds.

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(*iv*) Interest payable on National Savings Certificates (5th, 6th and 7th issue).

(*v*) 7-year National Savings Certificates (Fourth Issue).

(*vi*) Debentures issued by any co-operative society or any other institution notified by the Central Government; or

(*vii*) $6^1/_2$% Gold Bonds, 1977 or 7% Gold Bonds, 1980, where the bonds are held by an individual, not being a non-resident and the holder thereof makes a declaration in writing before, the person responsible for paying the interest that the total nominal value of Gold Bonds held by him did not exceed Rs. 10,000 at any time during the period to which the interest relates; or

(*viii*) Any other security of the Central or State Government where the security is held by an individual, not being a non-resident, and the holder thereof makes a declaration in writing before the person responsible for paying the interest that:

(*a*) he has not previously been assessed under the Indian Income-tax Act, 1961;

(*b*) his total income of the previous year in which the interest is due is not likely to exceed the maximum amount not chargeable to tax;

(*c*) the total nominal value of the securities held by him including such securities, if any, are held on behalf of any other person, did not exceed Rs. 2,500 at any time during the said previous year.

(*ix*) Any interest on such securities of the Central or State Government, paid to such class of persons and subject to such conditions as the Central Government may notify.

With effect from 1.6.1997 clauses (*viii*) and (*xi*) are being omitted and there will be no TDS on security issued by Central or State Govt.

No deduction of tax at source in case of interest on debentures [Section 193 (v)]

In case following conditions are fulfilled, the issuing authority will *not deduct any tax at source* with effect from 1-6-1989:

(*i*) Debentures are issued by a company in which the public are substantially interested;

(*ii*) Interest is paid to a Resident debenture-holder;

(*iii*) Debentures are listed on a recognised stock exchange;

(*iv*) Interest is paid by the company in account payee cheque; and

(*v*) The total amount of interest payable in the financial year, does not exceed Rs. 2,500.

Rates of tax deducted at source during the Financial Year 1996-97

Type of Income—For Residents	*Rate of Tax*
(*i*) Interest on any security of the Central or a State Government.	10%
(*ii*) Any debentures or other security for money issued by or on behalf of a local authority or a corporation established by a Central, State or Provincial Act.	10%

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(*iii*) Any debentures issued by a company where such debentures are listed in a recognised stock exchange in India in accordance with the Securities Contract (Regulation) Act, 1956 and any rules made thereunder. 10%

(*iv*) Interest on time deposits with a bank : 20% for domestic companies and 10% for all other resident assessees.

(*v*) Income credited or paid by Mutual Funds or U.T.I. under a particular scheme : 20% for domestic companies and 15% for all other resident assessees.

Both the above provisions have come into effect from 1.7.95.

(*vi*) On any other interest on security. 20%

For non-Residents

(*i*) On income by way of interest on a tax-free Govt. Security. 15%

Types of Securities

A. Exempted from Tax. Income-tax Act, 1961 provides for exemption of certain interest from tax u/s 10(15). Interest on all such securities, certificates, bonds etc. is altogether not included in the gross total income of the assessee and no tax is payable there upon.

There are some securities whose interest is exempted from tax but these are no longer in existance. These are:

(*i*) National Plan Certificates;

(*ii*) National Defence Bonds;

(*iii*) Treasury saving deposit certificates;

(*iv*) Special Bearer Bonds 1991.

Interest on following bonds issued by public sector Companies/undertakings has been notified to be exempted:

(*i*) 10% Secured Redeemable NTPC Bonds, 1986 (1st Series).

(*ii*) 10% Secured Redeemable non-convertible Bonds issued by Mahanagar Telephone Nigam Ltd.

(*iii*) 10% Secured Redeemable non-convertible Bonds issued by Indian Railway Finance Corp. Ltd.

(*iv*) 9% Secured Redeemable non-convertible Bonds 1987 (B Series) issued by National Hydro-electric Power Corp. Ltd.

(*v*) 9% Secured Redeemable non-convertible Bonds issued by Indian Railways Finance Corp. Ltd.

(*vi*) 9% (tax-free) Secured Redeemable Bonds issued by Power Finance Corp. Ltd.

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(*vii*) 10% (tax-free) Secured Redeemable non-convertible Bonds issued by Indian Telephone Industries Ltd.

(*viii*) 10 years—9% (tax-free) Secured Redeemable non-convertible NTPC Bonds—IVth Issue (private placement).

(*ix*) 10 years—9% (tax-free) Secured Redeemable non-convertible PFC Bonds—II Series (private placement) issued by Power Finance Corp.

(*x*) 10 years—9% (tax-free) Secured Redeemable non-convertible REC Bonds, issued by Rural Electrification Corp. Ltd.

(*xi*) 10 years—9% (tax-free) Secured Redeemable non-convertible Bonds (C Series) issued by Neyveli Lignite Corp. Ltd.

(*xii*) 7% Capital Investment Bonds.

(*xiii*) 9% or 10% National Relief Funds.

B. Tax free securities

(*a*) *Tax-free Commercial (Non Govt.) Securities.* These securities are those which are issued by a local authority, Statutory corporation or a company in the form of debentures or Bonds. Actually, these are not tax-free. Tax is paid by the issuing authority to the Government on behalf of such security-holders. The person who is holder of such security is liable to tax not only for the interest he is to receive but also the amount of tax which has been deposited on his behalf. The amount of interest actually received by holder is the net interest, *i.e.*, after deduction of tax at source. We have to find out the gross interest, *i.e.*, before deduction of tax, to include it is the gross total income of assessee. It can be done in the following manner :

$$\text{Grossing up} = \text{Net Interest received} \times \frac{100}{(100 - \text{rate of tax})}$$

Illustration 2. Mr. A invested Rs. 1,00,000 in 7% tax-free debentures of a company. What will be his taxable interest for the previous year ending on 31-3-97 if the rate of deduction of tax at source is @ 20%.

Solution

$$\text{Net Interest due} = 1{,}00{,}000 \times \frac{7}{100} = \text{Rs. } 7{,}000$$

$$\text{Grossed up} = 7{,}000 \times \frac{100}{(100 - 20)}$$

$$= 7{,}000 \times \frac{100}{80} = \text{Rs. } 8{,}750.$$

Interest to be added in gross total income of Mr. A for the previous year ending on 31-3-97 shall be Rs. 8,750.

(*b*) *Tax free Govt. Securities.* These securities are no longer in existance. Even if, these are issued then no tax is deducted at source. Otherwise it has same treatment as in case of less tax securities.

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Q. No. 2

Mr. R held the following investments :—

(*a*) Rs. 90,000 10% (Tax free) Debentures of a listed company, (Rate of T.D.S. 10%)

(*b*) Rs. 1,00,000 12% (Tax free) Panjab Govt. Loan.

Compute his income from interest on securities for the year ending 31.3.97.

[**Hints :** Taxable interest (*a*) Rs. 9,000 × 100/90 = 10,000 + (*b*) Rs. 12,000 Total Interest Rs. 22,000]

C. Less Tax Securities. This is the most common form of securities. Out of the amount of interest due to a security-holder, tax at the prescribed rates has to be deducted by the issuing authority before payment of interest. The assessee is to pay tax not only on the net amount of interest received, but he shall be liable to pay tax on gross interest, *i.e.*, amount due before deduction of tax at source. When the face value of securities and the rate of interest is given, it will directly give us the gross interest which we shall include in his gross total income, *e.g.*, 50,000, 6% port Trust Bonds.

Gross interest due = 3,000. It shall be fully added in the Gross Total Income of such person.

Sometimes only the amount of interest received by assessee is available and this interest is net interest, *i.e.*, after deduction of tax at source. In such a case we shall have to gross it up in the following manner.

Gross Interest = net Interest × 100/(100 – rate of tax), *e.g.*, if net interest is Rs. 1,600 gross interest will be Rs. 1,600 × 100/(100 – 20) = 2,000.

5. **Income from letting of plant, machinery or furniture.** If an assessee owns plant, machinery or furniture and it is let out to some other person, the rent so received by the assessee shall be chargeable to tax under this head provided letting of plant and machinery is not the business of the assessee.

If the assessee is engaged in the business of letting out plant, machinery or furniture, the rent so received shall be chargeable to tax under the head 'profits and Gains of Business or Profession.'

6. **Income from letting of plant, machinery or furniture with building.** The rent from a property is taxable under the head 'Income from House Property' but when an assessee lets out plant, machinery or furniture which is inseparable from building, the rent of building so received will be taxable under the head 'Income from Other Sources'. The letting of plant, machinery or furniture should not be the business of the assessee.

7. Any sum received under a Keyman Insurance Policy including any sum allocated by way of bonus [u/s 2(24) (xi)] if such amount is not taxable under the head "Profits and gains of business and profession" or under the head "Salaries".

Deductions [Section 57]

The taxable income under the head 'income from Other Sources' shall be computed after allowing the following deductions as provided in section 57:

1. *In case of Dividends and Interest on Securities.* From the dividend income, a deduction shall be allowed in respect of any sum spent by way of commission or

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remuneration to a banker or any other person as collection charges for realising the dividend or Interest on Securities.

2. *In case of Income from letting of machinery, plant or furniture with or without building.* The following deductions shall be allowed from the income earned by letting of machinery, plant or *furniture with or without building.*

(*i*) Expenditure incurred on current repairs of plant, machinery, furniture or building.

(*ii*) Insurance premium paid regarding these assets.

(*iii*) Depreciation on plant, machinery and furniture. Depreciation in respect of buildings will be allowed only if the assessee is the owner. It will not be allowed if the assessee is lessee or mortgagee in possession of the building.

3. *Deduction of amount deposited* [57 (*ia*)]

Any amount received by employer from his employees as their contribution of provident fund, E.S.I. Fund or superannuation fund is deemed as income u/s 59(*ic*) if not taxable under the head "profits and gains of business or profession".

In case employer deposits any amount (out of these incomes) in these funds before prescribed due date, such amount is allowed as deduction u/s 57 (*ia*).

4. *Standard Deduction out of Family Pension* [Section 57 (*iia*)]

In case of income in the nature of family pension, a deduction of a sum equal to $33^1/_3\%$ of such income or Rs. 12,000 whichever is less, shall be allowed [*With effect from assessment year 1998-99 this limit is being raised to Rs. 15,000 p.a.*]

Family pension means a regular monthly amount payable by employer to the legal heirs of deceased employee.

5. *Deduction from any other income.* Any expenditure which is spent to earn an income changeable to tax under this head shall be deducted from such income.

This deduction is not admissible to assessee being a foreign company.

The assessee, M/s Laxmi Agents Pvt. Ltd., Jamanagar, was doing agency business. The assessee borrowed money which was invested to purchase shares of a company which was managed by M/s Laxmi Agents Pvt. Ltd. The Gujarat High Court decided in the case of *Laxmi Agents Pvt. vs. The Additional Commissioner of Income-tax* that since the money was borrowed to purchase shares, so the interest paid on borrowed money shall be allowed as deduction out of dividend income, *i.e.*, it is an allowed deduction of "Income from other Sources". The interest paid on borrowed money cannot be charged against the business income of the assessee.

To claim this deduction following conditions must be satisfied:

(*i*) The expenditure should be incurred solely for earning such income.

(*ii*) It should not be in the nature of capital expenditure.

(*iii*) It should not be in the nature of personal expense.

(*iv*) It should be incurred in the relevant accounting year.

6. *Deduction from royalties received by authors.* (Other than those writing for films)—Actual expenses can be claimed as deduction.

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Amount Expressly Disallowed [Section 58]

The following expenses are not allowed to be deducted from such income:

In case of any assessee—(*i*) any personal expenses of the assessee.

(*ii*) Any interest chargeable under this Act which is payable outside India on which tax has not been paid or deducted at source.

(*iii*) Any payment which is chargeable under the head 'Salaries' if it is payable outside India unless tax has been paid or deducted at source.

(*iv*) In case an assessee has income from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever, such assessee shall not be allowed any deduction in respect of any expenditure or allowance in connection with such incomes.

This provision has come into force from 1-4-87, *i.e.*, assessment year 1987-88 but is not applicable in computing the income of an assessee being the owner of the horses maintained by him for running in horse races, from the activity of owning and maintaining such horses.

In case of every assessee any payment to relatives and associates made in cash may be disallowed under section 40A in certain circumstances. The provisions of section 40A are made applicable under this head also by sub-section 2 of section 58.

Illustration 3. Mr. X has the following incomes during the year ending 31.3.1997.

	Rs.
1. Dividend declared by M. Co. on 31.3.96	6,000
2. Dividend declared by Z Co. on 31.3.97	9,000
3. Interim dividend declared by X. Co. on 15.3.1996 but warrants were received on 1.6.1996	3,000
4. He won gold worth Rs. 1,00,00,000 from Panjab State Lottery	
5. During March 1997 he received Rs. 60,000 as winning from horse races. These horses are owned by him and expenditure incurred on maintenance of these horses amounted to Rs. 1,60,000.	

Compute income from other sources for the assessment year 1997-98.

Solution. *Computation of income from other sources*

		Rs.
Dividend		
(*a*) Declared by M. Co. on 31.3.96 [Not taxable in 96-97]		Nil
(*b*) Declared by Z. Co. on 31.3.97 Taxable		9,000
(*c*) Interim Dividend declared by X Co. on 15.3.96 but received on 1.6.96 Taxable in the year of receipt.		3,000
Winnings from Lottery		
Gold from Panjab State Lottery	10,00,000	
Less : exemption u/s 10(3)	5,000	9,95,000

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Winning from Horse races		
Received Rs. 60,000 Gross [60,000 × 100/60]	1,00,000	
Less expenses on maintenance of these horses	1,60,000	
Loss to be carried forward	60,000	Nil
Income from other sources		10,07,000

Q. No. 3

Compute income from other sources from particulars given below :

	Rs.
1. Interest on deposits with a company	10,000
2. University remuneration for working as examiner	6,000
3. Royalty for writing books	60,000
He claims to have spent Rs. 20,000 on writing these books	
4. Dividend declared by R. Co. on 1.3.97 but paid on 1.5.97	6,000
5. Interim dividend declared on 1.3.96 but paid on 1.6.96	3,000
6. Winning from horse races—amount received	90,000
Horses are maintained by him and expenses on maintenance of these horses are	2,40,000
7. Family pension received	36,000

[**Hints :** General Incomes u/s 56(1) Rs. 80,000
Specific incomes u/s 56(2) Rs. 9,000
Exp. on horses to be c/f Rs. 90,000]

Profits Chargeable to Tax [Section 59]

Under section 59(*i*) the provision of sub-section (1) of section 41 have been made applicable in computing the income of an assessee under section 56 as they are applicable in computing the income under the head "Profits and Gains of Business or Profession".

This provision deals with any allowance or deduction which has been allowed under this head in the assessment of income in any earlier year in respect of any expenditure, loss or trading liability incurred by the assessee subsequently during any previous year, the same amount is received or recovered in cash or in any other manner shall be deemed to be the income of that previous year in which it is recovered irrespective of the fact whether the source of income continues to exist in that year or not.

Avoidance of tax by certain transactions in securities (Bond Washing) [Section 94]

1. In case a person sells his securities to another person a few days before the accrual of interest and purchases them back after the date of accrual, and Assessing Officer is satisfied that the transaction has been made with the intention of avoiding tax, such interest shall be deemed as income of the transferor and not transferee.
2. In case a person has any beneficial interest in any securities and as a result of some arrangement either no income is received by such person

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or the income received by him is lower than the amount which he would have received, the interest, which would have accrued on such securities had there been no such arrangement, would be included in the income of person making such arrangement.

3. The above provisions will not be applicable, if such person proves to the satisfaction of the Assessing Officer that the transaction has not resulted into any avoidance of tax or if at all there was some avoidance it was exceptional as there had not been any avoidance of tax in any of three preceding previous years.
4. In case of dealer of securities, if there is a transaction of sale or purchase of securities and as a result the interest becomes receivable by him but is not deemed to be his income due to the above provisions, no account shall be taken of the transaction in computing profits arising from or loss sustained in the business.
5. The Assessing Officer may direct any person to furnish a detail of securities held by him by serving upon him a notice for not less than 28 days.

Accounting Methods [Section 145]

1. Income taxable under the head "Profits and gains of business or profession" or under "Income from other sources" may be computed in accordance with cash system or mercantile system of accountancy which is regularly employed by the assessee.
2. The Central Government has assumed the power to notify the various accounting standards to be followed by any class of assessees or in respect of any class of incomes.
3. In case Assessing Officer is not satisfied about the correctness or completeness of the accounts of the assessee, or assessee has failed to follow the method of accounting or has not followed the accounting standards as notified, the Assessing Officer may proceed to make best judgement assessment.

Various Accounting Methods

1. *Cash Method.* Under this system only such transactions are recorded in which actual receipts and actual payments of the business occur. Entries in the book are made only when money is actually received or is actually paid. No account is maintained for outstanding, prepaid, accrued or unearned incomes. This system is best suitable for professional persons like doctors, chartered accountants etc.

2. *Mercantile System.* In this system proper record of cash as well as credit transactions is made. Under this system any income which relates to the current year whether it is received or not and any expenditure whether actually paid or not, is taken into consideration for computing the profits and losses of the business. The profit and loss account prepared under this system shows correct profits and losses and balance sheet gives correct financial position of the business.

3. *Hybrid System.* Under this system of accounting, the assessee adopts both the previous methods in a mixed form. Some transactions are recorded in cash system and some under mercantile system depending upon the choice of book-keeper.

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The Income-tax authorities accept all the three methods of accounting for the purpose of assessment of profits and Gains.

The accounting system once adopted cannot be changed without the prior approval of Income-tax authorities. He will have to adopt his accounting method on regular basis and not merely for one particular year.

CHART SHOWING THE COMPUTATION OF INCOME FROM OTHER SOURCES

Items	*Treatment*
1. Residuary Head (General Incomes) (u/s 56(1))	Any income which does not come under any other head is included in this head, *e.g.*, any receipt from person other than employer, remuneration received by a teacher for university work, royalty, director's fee, sitting fee, agricultural income from outside India, interests (other than interest on securities) income of other persons to be included in the income of individual u/s 60-64 etc.
2. Specified incomes [u/s 56 (2)]	The Following incomes have to be included under this head: (*i*) dividends; (*ii*) Any annuity (due u/s 280); (iii) any winning from (*a*) Lottery (*b*) Races including horse races (*c*) Crossword puzzles; (*iii*) (*a*) employer's contribution to P.F., E.S.I. Fund etc., (*d*) interest on securities (*e*) Card games, and (*f*) Gambling and betting; (*iv*) Income from letting on hire any plant and machinery where it is not the business of assessee to do so; and (*v*) Income from letting on hire any building in which plant and machinery [as mentioned in (*iv*)] is situated and letting is inseparable from letting of plant and machinery.
3. Deductions (u/s 57)	(*i*) *for dividends and interest on securities* Any amount spent by way of collection charges. (*ii*) *For Letting of Plant and Machinery and Building*—Expenditure on current repairs, depreciation, insurance premium, etc., relevant to the period of letting. (*iii*) *for any other income*—Any expenditure wholly and exclusively for the purpose of earning such income such as interest on loan etc. (*iv*) Any amount deposited before due date with P.F., E.S.I. Fund etc. (*v*) *for royalties from books*—Actual exp. are allowed to be deducted. (*vi*) Standard deduction @ $33^1/_3\%$ or Rs. 12,000 p.a. whichever is less is allowed out of family pension.
4. Deduction of tax at source during financial year 1996-97	(*i*) Dividend @ 20% (in certain cases only. (*ii*) Winning from Lotteries 40% (if price exceed Rs. 5,000). (*iii*) Race course winning 40% (if prize exceeds Rs. 2,500). (*iv*) Interest of Securities 10% and 20%. (*v*) In case of interest on term deposits with banks—10% if interest exceeds Rs. 10,000. (*vi*) In case of income from U.T.I. or Mutual Funds exceeds Rs. 10,000. Chandigarh.

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Illustration 4. The following investments are held by Mr. Laxman on 1-4-1996 :

(*a*) Rs. 40,000, 10% U.P. Government Loan

(*b*) Rs. 35,000, 8% Preference Shares of a Sugar Mill Co.

(*c*) Rs. 50,000, 12% Debentures of Ugly Trading Co.

On 1-9-96, he sold the debentures-cum-interest and purchased Rs. 60,000, 15% debentures-cum-interest of Beauty Trading Co. Interest and dividend on investments is received half-yearly on 1st July and 1st January every year. Calculate income from securities for the previous year 1996-97.

Solution

Computation of Income from other sources : Interest on Securities

	Rs.
(*a*) Rs. 40,000, 10% U.P. Govt. Loan	4,000
(*b*) Rs. 50,000, 12% Debentures of Ugly Trading Co. (for six months due on 1st July, 1996)	3,000
(*c*) Rs. 60,000, 15% Debentures of Beauty Trading Co. (for 6 months due on 1st Jan., 1997)	4,500
Gross Interest	11,500
Deductions	Nil
Income from Interest on securities	11,500
Dividend	
Rs. 35,000, 8% Preference shares of a Sugar Mill	2,800
Income from other Sources	14,300

Q. No. 4

Compute income from other sources of Mr. Krishna Murthy who held the following investments during the previous year 1996-97.

(*i*) Rs. 11,000, 10% Central Government, Securities.

(*ii*) Rs. 32,000, 10% Tax-free commercial securities.

(*iii*) Rs. 6,300, received as interest of Tax free public limited company securities (listed).

(*iv*) Rs. 7,200, received interest on Karnataka Government securities.

(*v*) Rs. 3,600, received as interest on Deepak Fertilizers (listed).

(*vi*) Rs. 30,000, 13.5% securities on a paper mill co. limited (listed).

(*vii*) Rs. 35,000, 11% securities on a paper mill co. (listed).

(*viii*) Rs. 10,000, 15% Jaipur Municipal Corporation bonds.

(*ix*) Dividend received from Carona Ltd. Rs. 3,200

(*x*) During the year he also got a prize in Karnataka State Lottery. The net amount received by him was Rs. 30,000. Interest on all securities is payable on 1st July and 1st Jan. every year. Bank charges Rs. 200 as collection charges. *[Bangalore B.Com. Nov. 1994]*

[Hints : Income from other sources Rs. 82,300]

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Illustration 5. Harikrishnan, a resident individual, submits the following particulars of income for the previous year ending March 31, 1997 :

Dividend from REC International Ltd. (Gross) : Rs. 4,800. Dividend from Sundaram Finance Ltd. (net) Rs. 2,700 (tax deducted at source @ 20 per cent) interest paid on capital borrowed for the purpose of investment in shares of Sundaram Finance Ltd. Rs. 4,200. Collection charges in respect of dividend Rs. 160.

Winnings from lottery net amount Rs. 60,000 Tax deducted at source Rs. 40,000 Winnings from card games : Rs. 23,500. Interest on securities issued by the Government of Singapore Rs. 20,570.

Determine the income chargeable under the head "Income from other sources" for the assessment year 1997-98. *(B.Com. Madurai, April, 1993)*

Solution

Computation of Income from Other Sources

			Rs.	Rs.
I.	*General Income 56 (1)*			
	Interest on securities issued by Govt. of Singapore			20,570
II.	*Specific Incomes 56 (2)*			
	(*i*) *Dividend*			
	(*a*) R.E.C. International Ltd.		4,800	
	(*b*) Sundaram Finance Ltd. [Rs. 2,700 × 100/80]		3,375	
	Gross dividend		8,175	
	Less expenses—			
	(*a*) Interest on loan Rs.	4,200		
	(*b*) Collection charges Rs.	160	4,360	
	(*ii*) *Casual Incomes*			3,815
	(*a*) Winning from lottery (Rs. 60,000 + 40,000)		1,00,000	
	(*b*) Winning from card games		23,500	
	Gross		1,23,500	
	Less Exemption u/s 10 (3)		5,000	
				1,18,500
	Income from other Sources			1,42,885

Q. No. 5

Sri Mukunda furnishes the following particulars of the incomes for the previous year 1996-97. Compute his total income :

	Rs.
(*i*) Dividend Equity (gross)	600
(*ii*) Dividend on preference shares (net)	3,200

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(*iii*)	Income from letting on hire of building and machinery-composit lease	17,000
(*iv*)	Interest on bank deposits	2,500
(*v*)	Director's sitting fees	1,200
(*vi*)	Ground Rent	600
(*vii*)	Income from undisclosed sources	10,000
(*viii*)	Income from lotteries (gross)	10,000

The following deductions are claimed by him:

(*a*) Collection charges of dividend Rs. 20

(*b*) Allowable depreciation on buildings and machinery Rs. 4,000

(*c*) Fire Insurance on building and machinery Rs. 100.

[Bangalore B.Com. April, 1995]

[**Hints :** Income from other sources Rs. 36,780]

Illustration 6. R. Lakshmi has the following investments and incomes in the previous year ended 31-3-1997. Calculate her income from Other Sources.

	Rs.
(1) Dividend from a company (Gross)	7,800
(2) Examinership remuneration	2,000
(3) Royalty by the publication of a book	48,000
(4) Winnings from Lottery (Net)	30,000

(5) Rs. 40,000, 10% Debentures of company (Listed)

(6) Rs. 40,000, 12% Tax-free Panjab Govt. securities

(7) Rs. 50,000, 13% Less Tax commercial securities

(8) Rs. 40,000, 10% Tax-free debentures of a company

(9) Rs. 3,600, as interest on Tax-free debentures (not listed)

In July, 1996 she sold the above Rs. 40,000, 10% (tax free) debentures of a company for Rs. 45,000. In August, 1996 she inherited Rs. 60,000, 15%. Preference shares of XY Co. Ltd., from her father.

Interest and dividend on above securities will fall due on June 30th and December 31st of every year.

She claims the following deductions :—

(*i*) Collection charges for interest and dividend @ 2% of net amount realised

(*ii*) Purchase of lottery tickets Rs. 2,000.

Solution

Computation of Income from other Sources of Mrs. R. Lakshmi

Particulars	*Rs.*	*Amount Rs.*
General Incomes 56 (1)		
Royalty from Books	48,000	
Examinership remuneration	2,000	50,000
Specific Incomes 56 (2)		
(*i*) Dividend (*a*) on preference shares	9,000	
(*b*) from Indian Companies	7,800	16,800

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(*ii*) Winnings from Lottery [30,000 × 100/60]			50,000	
Less exemption u/s 10 (3)			5,000	
				45,000
(*iii*) Interest on Securities	*Gross Interest*	*Rate of Tax*	*Tax*	
Rs. 40,000, 10% listed Debentures	4,000	10%	400	
Rs. 40,000, 12% (Tax free) Govt. Secu.	4,800	—	—	
Rs. 50,000, 13% (Less Tax) Commercial securities	6,500	20%	1,300	
Rs. 40,000, 10% (Tax free) Commercial securities (6 months) [2,000 × 100/80]	2,500	20%	500	
Received Rs. 3,600 as interest on Tax free unlisted debentures [3,600 × 100/80]	4,500	20%	900	
Gross Interest	22,300		3,100	22,300
Gross Income from other sources				1,34,100
Deduction : Collection charges 2% [(22,300 – 3,100) + (16,800 – 3,360)]				653
Income from other sources				1,33,447

Note : No deduction of expenses on purchase of Lottery tickets.

Q. No. 6

Compute "Income from other sources" of an assessee.

1. Dividends received Rs. 9,600 on the shares of A Co. Ltd.
2. Dividends collected by Banker Rs. 4,800 on the shares of B Co. Ltd.
3. Dividends declared but not received on shares of C Co. Ltd. Rs. 8,500.
4. Bonus shares worth Rs. 1,000 received on equity shares of E. Co. Ltd.
5. Dividends Rs. 7,500 from F Co. Ltd. and latter on it was found that the dividends are paid out of capital.
6. Royalty from books Rs. 12,500 and the cost of preparing the manuscript is Rs. 3,125.
7. Winning from state lottery received Rs. 30,000.
   Collection charges for dividends Rs. 180 and amount spent to buy lottery ticket during the previous year was Rs. 3,000.

[Bangalore B.Com. Oct., 1995]

[**Hints**: Dividend on reduction of capital is taxable; Income from other sources Rs. 88,195]

Q. No. 7

Keshav borrowed Rs. 24,000 on 1-6-1996 from bank at interest of 10% P.A. He invested the money in purchase of equity shares of a Public Ltd. Company. During the year, no dividend was received from the company. Keshav, however, claimed that interest paid to the bank must be allowed as expense. How will you decide the claim?

[C.A. (Inter), 1979]

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[**Hint.** Supreme Court has held in a case *C.I.T. v. Rajendra Prasad Moody (1978) 115 I.T.R. 519 (S.C.)* that interest paid shall be allowed as deduction u/s 57 (*iii*) if the money was borrowed for investment in shares and it is also immaterial whether during the accounting year those shares have yielded any return in the shape of dividend or not. Loss under the head 'Income from Other Sources' shall be adjustable against any income under any other head in the same assessment year (Sec. 71)]

Q. No. 8

Sharath holds 5,000 equity shares in a Public Limited Company. For its year ending 30-9-1995, the company declared a final dividend of Rs. 3 per share at the Annual General Meeting held on 15-3-1996. For the year ending 30-9-1996, the Board of Directors at their meeting held on 31-1-1997 declared an interim dividend of Rs. 2 per share. Both the dividend warrants were received by Sharath on 30-4-1997. Discuss the assessment years in which the above dividends will be taxed. *[C.A. Inter]*

[**Hints.** Dividend of Rs. 15,000 taxable in previous year 1995-96 as it was declared on 15-3-1996, Interim dividend of Rs. 10,000 received on 30-4-1997 is taxable in the previous year 1997-98]

Q. No. 9

Following are the incomes of Sri Amar for the financial year 1996-97. Compute his taxable income under the head "Other Sources" if he is Resident, NOR, or Non-resident :—

	Rs.
(*a*) Interest on Saving Bank deposit A/c with Union Bank, Delhi	1,000
(*b*) Income from agriculture in Africa invested in Pakistan	40,000
(*c*) Dividends received in USA from an American company part of which Rs. 4,000 remitted to India	12,000
(*d*) Family pension received in Kenya for services rendered in India	24,000

[**Hints.** Income from other Sources if Resident Rs. 69,000 ; if NOR or NR Rs. 17,000 out of pension standard deduction @ $33^1/_3\%$ is to be allowed]

Q. No. 10

Mr. Basu *received* the following incomes during 1996-97. Compute taxable income under "Other Sources" separately for each case :—

	Rs.
A. (*i*) Winnings from Sikkim lottery	12,000
(*ii*) Winnings from Horse races	2,000
(*iii*) Winnings from crossword puzzle	4,000
(*iv*) Winnings from card games	10,000
B. (*i*) Winnings from lottery	2,000
(*ii*) Winnings from horse races	18,000

[**Hints.** A. Lottery Rs. 12,000 × 100/60 = Rs. 20,000 Gross Income Rs. 36,000 less exemption u/s 10(3) Rs. 5,000; No. T.D.S. in card games.
B. Race winnings Rs. 18,000 × 100/60 = Rs. 30,000 Gross Income Rs. 32,000 exemption u/s 10(3) Rs. 4,500]

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Q. No. 11

Mr. X, who maintains books of accounts on merchantile basis borrowed Rs. 20,000 at 18% p.a. on 1-9-1996 and invested it in 12% securities of the Central Govt. purchased at Rs. 100/- with due date of interest on 1st January and 1st July every year. On 31-7-96 he borrowed Rs. 30,000 @ 15% p.a. for investing it in 14% listed debentures of C Ltd. with date of payment of interest being 15th May every year. Interest on borrowings for the period ending 31-3-97 is, however, paid by X on 15-4-97. He pays 2% commission to his bank on amount of interest realised. Compute his income chargeable under the head 'Income from Other Sources'.

[C.A. Inter May, 1992 (Adapted)]

[**Hints.** Interest on Central Govt. Securities Rs. 1,200; Interest on debentures of C Ltd. NIL, deduction of interest Rs. 2,100 + Rs, 3,000 and Collection charges Rs. 24. Loss under the head, Other Sources Rs. 3,924 to be set off from income under any other head.] [P-8].

Q. No. 12

From the following information compute the income from other sources for the assessment year 1997-98 :

	Rs.
(*i*) Card games loss	12,000
(*ii*) From the activity of owning and maintaining horses for race purposes	
(*a*) Loss at Bombay	40,000
(*b*) Profit at Bangalore	20,000
(*iii*) Dividend (Gross) from Indian Companies	6,000
(*iv*) Winnings from horse races	4,000

[**Hints.** Dividend Rs. 6,000 ; card games' loss can't be set off; loss of Rs. 20,000 from maintenance of horses to be set off from race winnings. Loss to be c/f Rs. 16,000]

Q. No. 13

From the following particulars for the Year ended 31st March, 1997, compute the income under the head "Income from Other Sources":—

	Rs.
Dividends (Net)	25,200
Dividends (Gross)	12,000
Collection charges in respect of Dividends	300
Rent from letting out of a building alongwith plant and machinery	30,000
Depreciation on buildings	4,000
Insurance on buildings	1,600
Office expenses relating to buildings	1,600
Repairs, rates etc.	1,600

[**Hints.** Income Rs. 64,400]

[Nagarjuna B.Com. Sept., 1995]

Q. No. 14

From the particulars of income of Sri. Madanmohan, compute his Gross total income for the Assessment year 1997-98 :—

(*i*) He owns an agricultural land in Bangladesh from which he earned on income of Rs. 6,500.

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(*ii*) He owns a plot of land in Dharwad which is let out for Rs. 1,200 p.m. for trading purposes.

(*iii*) He has a building near agricultural land in a village in India. It is let out for Rs. 900 p.m. and used for storing agricultural equipments and for supervision of agricultural work.

(*iv*) He received Rs. 12,500 during the year as management consulting fee.

(*v*) He has a quarry in Ankola. He has let it on a royalty of 50 paise per ton of stone raised. During the year 14,600 tons of stone was raised. He spent Rs. 450 to earn royalty.

(*vi*) He has let machinery and furniture at Rs. 3,000 p.m. He spent Rs. 1,000 on the repair of these assets. Depreciation allowed on these assets is Rs. 6,000.

(*vii*) He lives in a rented house paying a rent of Rs. 2,000 p.m. He has sublet 40% of this house at a rent of Rs. 1,500 p.m. He has paid Rs. 1,000 as municipal tax on the house and spent Rs. 500 on the repairs of the whole house.

(*viii*) He has received an amount of Rs. 60,000 as lottery prize. He borrowed Rs. 30,000 on 1-6-1996 from a bank at 18% p.a. interest. He invested the money in the purchase of equity shares of Public Limited Company. During the year he has not received any dividend from the company.

[Karnataka B.Com. April, 1995]

[**Hints :** House Property Rs. 8,640 Income from other sources Rs. 1,67,550]

Q. No. 15

From the following particulars of Mr. Edward for the previous year ended 31st March, 1997 compute his total Income for the Assessment year 1997-98.

He received :	Rs.
(*i*) Director's fee from a company	10,000
(*ii*) Interest on Bank Deposits	3,000
(*iii*) Income from undisclosed sources	12,000
(*iv*) Winning from lotteries (Net)	21,000
(*v*) Royalty on a book written by him	8,000
(*vi*) By giving lectures in functions	5,000
(*vii*) Interest on loan given to a relative	7,000
(*viii*) Interest on tax free debentures of a company (listed in recognised stock exchange) (Net)	3,600
(*ix*) Dividend on shares (Net)	6,400
(*x*) Interest on post office savings bank A/c	500
(*xi*) Interest on tax free Government Securities	2,200

He paid Rs. 20 for collection of dividend and Rs. 1,000 for typing the manuscript of book written by him.

[Karnataka B.Com. 1994]

[**Hints :** Income from other sources Rs. 88,180]

Q. No. 16

Hari Gopal is a member of Parliament from Bangalore. During the previous year 1996-97 he has the following incomes:

(*i*) As a member of Parliament he received a salary of Rs. 500 p.m. and daily allowance of Rs. 5,100 for attending the various sessions.

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(*ii*) He held the following investments:

(*a*) 10% preference shares in Mysugar Works Ltd., of the face value of Rs. 5,000.

(*b*) 1,000 equity shares of Rs. 10 each in Tata Finlay Ltd. The company declared interim dividend of 15% on 15th Feb., 1996 but paid on 1st May, 1996 and final dividend of 10% on 30-3-1997.

(*c*) A 10% fixed deposit of Rs. 10,000 is held by him in Indian Banks. Interest is credited annually.

(*d*) He received dividend of Rs. 500 from a Co-operative Society.

(*iii*) He won Rs. 8,000 in cross-word puzzles and horse races.

(*iv*) On 1-9-1996 he purchased a plot of land for constructing his house. On account of shortage of funds he could not get house constructed and hence let out the plot at Rs. 150 p.m. from 1-11-1996.

(*v*) He has let machinery and furniture and also building to Mr. Krishna at a monthly rent of Rs. 5,000. He spent Rs. 1,500 on the repair of machinery, furniture and building during the previous year. Depreciation allowed on these assets for the previous year was Rs. 10,000.

The bank charged 1% commission on collection of dividends. Compute the taxable income of Sri Hari Gopal under the head 'Income from Other Sources'.

[Mysore and Panjab (1985) B.Com.]

[**Hints.** All incomes are taxable under the head 'Other Sources'.]

(*i*) Salary Taxable; Allowance Exempted; (*ii*) Dividends 3,500 – 35 = 3,465; (*iii*) Rs. 8,000 – 5,000 = 3,000; (*iv*) Land Rent Rs. 750; (*v*) Machinery rent 60,000 (–)11,500 = Rs. 48,500. Total Rs. 61,715. [P-3)

Q. No. 17

Shri Swami Prasad furnishes the following particulars of his income for the previous year ending on 31st March, 1997 :

(*i*) Dividend from a tea company in May, 1996 Rs. 2,500 (gross) (60% of the income of the company is agricultural income).

(*ii*) Amount won on 1st November, 1996 from a horse race Rs. 6,500.

(*iii*) Interim Dividend declared by the Directors of K. Co. Ltd. in January, 1997 but the payment was received in June, 1997 for which dividend warrants were despatched in May, 1997. The amount received as dividends was Rs. 8,000.

(*iv*) Dividend declared by P. Co. Ltd., in January, 1997, dividend warrants were despatched in April, 1997 and the payment was received in June, 1997 amounting to Rs. 4,000 (gross).

(*v*) Amount received in March, 1997 in connection with winning from a lottery Rs. 30,000.

(*vi*) Interest (gross) on deposit with a firm Rs. 5,600.

(*vii*) Dividend received from a Co-operative Society, Rs. 450.

(*viii*) Income from non-agricultural land Rs. 1,500.

Shri Swami Prasad claims the following expenses:

Bank commission Rs. 1,000 for collecting dividends and interest and Rs. 500 on winnings from horse race, and winnings from lotteries; interest on loan taken to purchase shares in tea company Rs. 800; and expenses incurred for purchasing lottery tickets Rs. 2,000.

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Compute the taxable income of Sh. Swami Prasad under the head 'Income from Other Sources'. *[B.Com., Panjab]*

[**Hints.** Income from other sources Rs. 63,750; Interim dividend not received, hence not taxable; Expenses incurred for collecting race winning and horse races not allowed]

Q. No. 18

An assessee had the following investments as on 1st April, 1996 :

(*i*) Rs. 40,000, 12% Central Govt. Loan;
(*ii*) Rs. 30,000, 10% Govt. Securities;
(*iii*) Rs. 20,000, 9% Preference shares of Paper Mill Company;
(*iv*) Rs. 50,000, 11% Bombay Port Trust Bonds;
(*v*) Rs. 20,000, 15% Debentures of a limited company (unlisted);
(*vi*) Rs. 10,000, 10% Securities issued by Govt. of England;
(*vii*) Rs. 10,000, 9% National Relief Bonds;
(*viii*) Rs. 20,000, 14% Municipal Debentures;
(*ix*) Rs. 10,000, 12% National Savings Certificates (8th issue);
(*x*) Rs. 16,000, 10% (Tax-free) Debentures of a limited company (unlisted).

On 1st September, 1996 he bought Rs. 50,000, 12% Maharashtra Govt. Bonds for Rs. 60,000 the interest of which is payable on 30th June and 31st December. For this purpose he took a loan from his Bankers for Rs. 40,000 @ 15% p.a. and the balance of Rs. 20,000 were financed out of a previous loan taken for purchase of motor car @ 9% p.a.

Bank charged 2% of interest and dividend as collection charges and 3% commission on purchase of securities.

Calculate the income from other sources

[Adapted Calcutta Uni. B. Com. (Hons.)]

[**Hints.** Interest Rs. 1,000; Dividend Rs. 1,800; Interest on securities 25,300, Deductions 4,062; Income from other Sources Rs. 24,038] [P-7]

Q. No. 19

Mr. Shivanand has following investments in the previous year ended 31st March, 1997 :

(*i*) Rs. 11,000, 10% Karanataka State Govt. Loan.
(*ii*) Rs. 30,000, 13.5% Debentures of Lohia Machine Tools Ltd. (Listed).
(*iii*) Rs. 35,000, 11% Securities of Sugar Mill Company (not Listed).
(*iv*) Rs. 31,600, 10% Tax-free Commercial Securities.
(*v*) Rs. 3,580, *received* as interest on Tamil Nadu Govt. Securities.
(*vi*) Rs. 3,555, *received* as interest on the Securities of a Paper Mill Company (not listed).
(*vii*) Rs. 4,474, *received* as interest on securities of Textile Company (listed).

During the previous year 1996-97 he purchased Rs. 50,000, 7% capital investment Bonds on 1st October, 1996. For this purpose he borrowed Rs. 30,000 from Bank at 15% p.a. Interest on all Securities is payable on 30th June and 31st December. The bank charged $1^1/_2$% commission on Net realisation of interest and dividend as collection charges.

He was also a Director in a company from which he received Rs. 3,000 as directors fees. His other incomes are:

(*i*) Winning from Lottery Rs. 25,000
(*ii*) Income from Agriculture in Sri Lanka Rs. 10,000

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(*iii*) Winnings from Horse race Rs. 15,000

(*iv*) Interest on Post office Savings Bank Account Rs. 2,000.

Find out his taxable income from other Sources for the Assessment Year 1997-98.

[Bangalore University, B.Com.]

[**Hints.** Interest on Securities (gross) Rs. 26,343 Tax at source Rs. 3,859 Deduction of collection charges Rs. 337; Casual Income Rs. 35,000; Income from Other Sources Rs. 74,006]

Q. No. 20

Karthik a resident individual, submits the following particulars of his income for the previous year ending March, 31, 1997 :

(*a*) Dividend from Goldern Finance Ltd. (Gross) Rs. 5,600. Dividend from Lakshmi Mills Ltd. (Net) Rs. 3,200. Interest paid on capital borrowed for the purpose of investment in shares of Sundaram Finance Ltd. Rs. 6,200. Collection charges in respect of dividend Rs. 125.

(*b*) Rent from letting a building alongwith plant and machinery (rent of building cannot be separated from rent of plant machinery) Rs. 31,200. Collection charges in respect of rent Rs. 400. Fire insurance premium in respect of building Rs. 550. Reparis in respect of building Rs. 4,800. Fire insurance premium in respect of plant and machinery Rs. 750. Depreciation of Building, Plant and Machinery Rs. 18,600.

(*c*) Winnings from card games Rs. 13,500. Winnings from lottery : Net amount Rs. 1,20,000 ; Tax deducted at source 40%.

(*d*) Interest on securities issued by the Government of Sikkim Rs. 20,000.

Determine the income chargeable under the head "Income from Other Sources" for the assessment year 1997-98. *[B.Com. Madurai Oct., 1994]*

[**Hints.** Dividend Rs. 3,275, Rent Rs. 6,100, Casual incomes Rs. 2,08,500, Interest on securities Rs. 20,000, Income from Other Sources Rs. 2,37,875]

Q. No. 21

Mr. Subramaniam furnished the following particulars of his investments for the previous year ended 31-3-97.

(*a*) (*i*) Rs. 30,000 units of UTI (dividend received Rs. 4,000).

(*ii*) Rs. 40,000 in Post Office S.B. A/c at 5% interest p.a.

(*iii*) Rs. 9,00,000 Fixed Deposit in Syndicate Bank at 11% interest p.a. made on 1-11-95. Amount of interest credited to his account.

(*iv*) Rs. 40,000 deposit in Panjab Finance Corporation at 13% interest p.a.

(*v*) Rs. 25,000, 10% debentures of Pfizer Ltd. (Listed)

(*vi*) Rs. 30,000, 10% Haryana Electricity Board Bonds.

(*vii*) Rs. 4,500 Interest received on National Development Bonds.

(*b*) On 1-11-96 he purchased Rs. 45,000, 7% Capital Investment Bonds for which he borrowed Rs. 30,000 @ 15% interest.

(*c*) On 25-4-96 he inherited Rs. 45,000, 10% Debentures of Bata Limited (Listed) from his uncle.

(*d*) The interest on all these securities is payable half yearly on 30th June and 31st December every year. The bank charged 1% commission on collection of net amount of interest and dividend.

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From the above compute his income from Other Sources and bank does not charge any commission on collection of interest on deposits with same bank.
[**Hints.** Interest on P.O.S.B. A/c Capital Investment Bonds exempted. No tax at source on Dividend of U.T.I., Int. on deposits with bank, PFC, National Development Bonds and on debentures of Pfizer Ltd. (amount upto 2,500) Gross Income Rs. 33,600; Deduction of collection charges Rs. 329]

QUESTIONS

1. Define the term 'Dividend' as given in section 2(22) of Income-tax Act, 1961. How is the dividend income put to tax under the provisions of this Act?
2. Mention the different kinds of incomes specifically mentioned as chargeable to tax under the head "Income from Other Sources".
3. Enumerate the items of deductions allowable in computing income from other sources.

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7 AGGREGATION OF INCOME

Income of other person—Income from firm and AOP— Clubbing provisions—Deemed Incomes—Questions.

While aggregating the income of an assessee, following are also included in the total income:

(*i*) Incomes of other persons to be included in the income of individual (Sections 60-50).

(*ii*) Income received from Firm assessed as firm and Association of Persons (Sections 66 and 67).

(*iii*) Deemed Incomes (Sections 68-69).

Incomes of other persons to be included in assessee's total income [Sections 60 to 65]

Sections 60 to 65 deal with such cases where a particular income is earned or received by another person and does not belong to the assessee but for income-tax purposes, such incomes are included in the total income of the assessee.

(1) Transfer of income where there is no transfer of assets [Section 60]

Under section 60 where the assessee transfers to another person some income but without the transfer of assets producing that income, such an income shall not be the income of the transferee but it shall be chargeable to income-tax as the income of the transferor and shall be included in his gross total income.

Such a transfer of income may be revocable or irrevocable and whether effected before or after the commencement of this Act.

(2) Revocable transfer of assets [Section 61]

All incomes arising to any person by virtue of a revocable transfer of assets shall be chargeable to income-tax as the income of the transferor and shall be included in his total income.

Section 63 has defined the words 'transfer' and 'revocable transfer' as under:

(*a*) A transfer shall be deemed to be revocable if—

(*i*) it contains any provision for the re-transfer directly or indirectly of the whole or any part of the income or assets to the transferor, or

(*ii*) it, in any way, gives the transferor a right to reassume power directly or indirectly over the whole or any part of the income or assets.

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(*b*) 'Transfer' includes any settlement, trust, covenant, agreement or arrangement.

Transfer Irrevocable for a Specified Period [Section 62]

Section 62 (1) lays down that the provisions of section 61, shall not apply to any income arising to any person in case the transfer falls under any of the following categories:

(*i*) By way of trust which is not revocable during the life time of the beneficiary and, in the case of any other transfer, which is not revocable during the life time of the transferee, or

(*ii*) Transfer made before the 1st day of April, 1961, which is not revocable for a period exceeding six years.

Provided that the transferor derives no direct or indirect benefit from such income in either case.

According to section 62(2) in the cases discussed above, all incomes arising to any person by virtue of such transfer shall be chargeable to income-tax as the income of the transferor or as and when the power to revoke the transfer arises and shall then be included in his total income.

(3) Income of Individual to include the income of his spouse from firm and from assets transferred, and income of minor child etc. [Section 64]

Apparently the following incomes belong to persons other than the assessee but these are included in the assessee's gross total income under Section 64. These incomes are:

(*i*) *Any salary, commission, fee or any other remuneration received by spouse* [Section 64 (1) (*ii*)]. Any income accrued to spouse by way of salary, commission, fee or any other form of remuneration whether in cash or in kind from a concern in which such individual has a substantial interest, shall be considered to be the income of such individual.

Substantial interest means having voting power in the company which is not less than 20% of equity capital or is entitled to at least 20% of profits of such concern.

Any income derived by spouse due to his technical or professional qualifications or professional knowledge or experience, it shall not be clubbed with the income of individual.

The word 'Spouse' means husband or wife, *i.e.*, husband is spouse for wife and wife is spouse for husband. Wife means a lawfully wedded wife.

(*ii*) *Income of spouse from assets transferred* [Section 64 (1)]. While computing the total income of any individual, the income in the following cases shall be included, as arising directly or indirectly:

(*a*) to the spouse of such individual from assets transferred directly or indirectly to the spouse by such individual otherwise than for adequate consideration or in connection with an agreement to live apart.

Consideration should be adequate, *i.e.*, equal or nearly equal to the value of assets transferred. According to a Supreme Court decision natural love and affection cannot constitute adequate consideration. The relationship must exist on the date of transfer.

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Assets transferred means when an individual purchases property in the name of his wife from his own funds. Any income from such transferred assets will be included in the income of the transferor.

If the assets are purchased from the income of the transferred assets any income to a spouse or from such assets shall not be included in the total income of tansferor.

If the wife purchases some assets out of the savings from her pocket money and those assets which were transferred to her before marriage, income from such assets shall be considered as her own income.

Provisions regarding clubbing of income of spouse derived from assets gifted to her by the other spouse are applicable only in respect of the income derived from such assets in the hands of spouse. But these provisions are not applicable to the income derived by spouse *from the income of such assets. [Popat Lal Dekam Chand v. C.I.T. (1950) Bom.]*

(iii) Income from assets transferred to son's wife without adequate consideration. [64(1) (vi)]

Any income accruing from asset which is transferred after 1-6-1973 to daughter-in-law without adequate consideration shall be considered to be the income of transferor w.e. from assessment year 1976-77.

(iv) Assets transferred for benefit of spouse [Sec. 64 (1)] *or for the benefit of son's wife [64(1) (viii)].* While computing the total income of any individual there shall be included such income as arises directly or indirectly to any person or association of persons from assets transferred otherwise than for adequate consideration to the person or association of persons by such individual to the extent to which the income from such assets is for immediate or deferred benefit of his or her spouse.

It simply means that when assets are transferred without adequate consideration to some person or association of persons, the ultimate benefit of which shall be of the spouse of the transferor, the income from such assets is considered to be the transferor's income and so added in his total income.

Where, from the assets transferred, only a portion of the income is meant for the immediate or deferred benefit of the spouse of the transferor, then only such income is to be added in the total income of the transferor. [Section 64(1) explanation 1]

(v) Investment of assets transferred without adequate consideration in business [64(1) explanation 3]

In case assets transferred directly or indirectly by an individual to his spouse or son's wife (to be referred as transferee) are invested by transferee—

(*i*) in any business, that part of the income arising out of the business to transferee in any previous year which is calculated as per proportion given below at (*ii*) shall be clubbed with the income of individual. Such investment in business must not be in the form of capital as a partner in the firm—

$$\text{Business Income} \times \frac{\text{Value of the asset on 1st day of previous year}}{\text{Total Investment in the business on 1st day of previous year}}$$

(*ii*) In case investment is made as contribution of capital as a partner in firm, the interest receivable by the transferee from the firm calculated in

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proportion given below shall be clubbed with the income of individual—

$$\text{Interest} \times \frac{\text{Amount invested out of asset}}{\text{Total capital invested by transferee in firm}}$$

(4) Income of Minor [Section 64(1A)]

Any income of a minor shall be clubbed with the income of that parent whose other income is higher (if marriage of the parents persists) or is the income of that parent who maintains such minor child (if marriage of parents does not persist). In case minor's income is included in the income of one of the parents, it will always be included in his income and shall not be included in the income of other parent unless Assessing Officer is satisfied that it is necessary to do so but after giving an opportunity of being heard.

The above provision is not applicable on any income of a minor which accrues or arises due to (*a*) manual work done by minor child or (*b*) activity involving application of his specialised knowledge and experience.

The Finance Act, 1992 has added this section from assessment year 1993-94.

U/s 10 (32), in case any income of minor child is clubbed with the income of either parent, such parent can claim an exemption of income so clubbed or Rs. 1,500 whichever is less.

With effect from assessment year 1995-96 income of a minor child who is suffering from any of the disabilities specified u/s 80 U, shall not be clubbed.

(5) Transfer of individual's self acquired property to the H.U.F of which he is a member [Section 64(2)]

U/s 64(2) where an individual converts his individual or self-acquired property into the common pool of H.U.F. of which he is a member after 31-12-1969, the income from such a converted property shall be treated as under:

(*a*) The individual shall be deemed to have transferred the converted property, through the family, to the members of the family for being held by them jointly.

(*b*) The income derived from the converted property or any part thereof shall be deemed to arise to the individual and not to the family.

(*c*) Where the converted property has been the subject-matter of a partition (whether partial or total) amongst the members of the family, the income derived from such a convered property as is received by the spouse or minor child on partition shall be deemed to arise to the spouse or minor child from assets transferred indirectly by the individual to the spouse or minor child and in such case the provision of Sec. 64(1) shall apply.

It is further provided that any income as under (*b*) and (*c*) if added in the total income of the individual, shall be excluded from the total income of the family, individual's spouse or minor child.

Benami Transactions

If a transaction is considered to be a *Benami* transaction, the income from such transaction shall be taxable in the hands of the real person and so the *benamider* is not taxed for the income arising from such transactions.

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Income received from AOP [Section 67A]

In the aggregation process of total income of the assessee following income is included in the total income of the assessee but this income is tax-free (Section 67A). It is—

> If the assessee is a member of an association of persons or a body of individuals other than Hindu Undivided Family, any portion of the amount which he is entitled to rebate on the income received from the association or body on which income-tax has already been paid by the association or body.

Member's share in the income of AOP (Section 67A). The detailed study of this point is given in the chapter 'Assessment of Firms' in Part IV of this book.

DEEMED INCOMES

(*i*) Cash Credits [Sec. 68]

Where any sum is found credited in the books of an assessee maintained for any previous year and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of assessee of that previous year. Such cash credits may be assessed either as business profits or an income from other sources. In the case of business community, it is normally considered as business profit. It will be taxed in the year in which such cash credits are detected.

If the assessee fails to submit any satisfactory explanation or the A.O. is not satisfied with the explanation, the income is treated as assessee's income from undisclosed sources.

(*ii*) Unexplained Investments [Sec. 69]

Where, in the financial year immediately preceding the assessment year, the assessee has made investments which are not recorded in the books of accounts and the assessee fails to furnish any satisfactory explanation as from where this money came or if the Assessing Officer is not satisfied with the explanation the assessee has furnished the value of such unexplained investment may be deemed to be the income of the assessee of such financial year.

(*iii*) Unexplained Money etc. [Sec. 69A]

Where, in any financial year the assessee is found to be the owner of any money, bullion, any jewellery or other valuable articles and all these valuable articles, money, bullion, jewellery etc. are not recorded in the books of accounts of the assessee, the assessee either does not furnish any explanation as to how he acquired these things or his explanation, if furnished, is not up to the satisfaction of the Assessing Officer, the money, and the value of the bullion, jewellery or other valuable articles may be deemed to be the income of the assessee for such financial year.

(*iv*) Account of Investment, etc. not fully disclosed in Books of Accounts [Sec. 69B]

In case the assessee acquired certain investments, jewellery, valuable article etc. and the actual money spent on these items is more than what is shown or

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recorded in his books of accounts and the assessee either does not furnish any explanation for this or with his explanation the Assessing Officer is not satisfied, the excess amount under section 69B may be deemed to the income of the assessee for such financial year.

(*v*) Unexplained Expenditure [Sec. 69C]

The Taxation Laws (Amendment) Act, 1975 has inserted this new clause with effect from 1-4-76. According to this provision, where in any financial year an assessee has incurred any expenditure and he offers no explanation about the source of such expenditure or part thereof or the explanation offered by him is not satisfactory according to the opinion of A.O., the amount covered by such expenditure or part thereof, as the case may be, is deemed to be the income of the assessee for such financial year.

(*vi*) Payment of Hundi Money in Cash [Sec. 69D]

This new clause has also been inserted by aforesaid Act from 1-4-77. According to this clause any amount borrowed on 'hundi' or 'repaid on hundi' otherwise than in *account payee cheque* drawn upon a bank, shall be deemed to be the income of the person borrowing or repaying the amount for the previous year in which such amount was borrowed or repaid. If the amount borrowed is taxed as deemed income under the provisions of 69D, it will not be taxed again when the amount is repaid.

Amount repaid shall include the amount of interest also.

Q. No. 1

How are following incomes treated under Income-tax Act, 1961?

(*a*) Mr. A gifted Rs. 1,00,000 to his son B on his 17th Birthday on 2nd Oct., 1995. The money was deposited in a Nationalised Bank @ 10% p.a. During the year ending on 31st March, 1997 B received Rs. 10,000 as interest income.

(*b*) A minor made a fixed deposit of Rs. 1,00,000 in a partnership firm in which his father and mother are partners. The deposit carries interest @ 20% p.a. The incomes of father and mother other than from the firm are Rs. 15,000 and 20,000 respectively.

[**Hints.** (*a*) Rs. 10,000 to be clubbed with A's income u/s 64(1A). (*b*) Rs. 20,000 is to be clubbed with mother's income].

Q. No. 2

Assessee was engaged to be married to R. The engagement was announced on 30-9-1995 and marriage took place on 15-10-1995. Assessee transferred to R on 12-10-1995 shares worth Rs. 1,00,000. R received Rs. 15,000 as dividend on these shares in Sept. 1996, I.T.O.'s. contention is that it is not R's income. Discuss whether I.T.O.'s contention is correct or wrong.

[**Hints.** No clubbing, R's income]

Q. No. 3

Mr. X gifted gold jewellery worth Rs. 1,00,000 to his wife Mrs. X on 1-1-90. It was acquired on same day. On 1-5-91 Mrs. X sold this jewellery for Rs. 1,50,000 and invested the same in a plot for Rs. 3,00,000. The remaining amount was paid by her out of her own funds. The plot was sold for Rs. 7,50,000 on 1-11-96.

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Compute the income chargeable to tax in the hands of Mr. X and Mrs. X on the sale of jewellery as well as plot if C.I.I. for 1989-90 is 172, for 1991-92 is 199 and for 1996-97 is 305 ?

[**Hints :** Previous year 1991-92 Mr. X's income = S.T.C.G. Rs. 50,000 Previous year 1995-96 Mr. X L.T.C.G. Rs. 1,45,100 as Mrs. X's L.T.C.G. Rs. 1,45,100]

Q. No. 4

Decide about the person in whose hands the following incomes shall be taxable :—

(*i*) Mr. Jeevan transfers 1000 debentures of Rs. 100 each carrying 15% interest to Mr. Ramesh on the condition that if price is not paid within 1 year, the debentures will revert back to Mr. Jeevan.

(*ii*) Master D. (Age 16 years) received following incomes during 1996-97 :—

	Rs.
(*a*) Interest on Bank deposits	6,000
(*b*) Interest on Debentures	8,000
(*c*) Dividend on shares of a company	9,000
(*d*) Income from a singing concert held by him	40,000
(*e*) His father's total income	69,400
(*f*) His mother's total income	69,500

(*iii*) Mr. S tranfers a shop (monthly rent Rs. 4,000) to his relative Mr. B on the condition that shop will revert back to Mr. S on the death of Mr. B.

[**Hints :** (*a*) Revocable Transfer—income of Rs. 15,000 to be clubbed with income of Mr. Jeevan; (*b*) Income to be clubbed with mother's income Rs. 6,000 + 8,000 + 9,000 (–) u/s 10(32) Rs. 1,500 = Rs. 21,500; mother can claim deduction u/s 80L; (*c*) Irrevocable transfer hence transferee's income]

QUESTIONS

1. Under what circumstances income of other persons can be included in the income of assessee under Income-tax Act, 1961 ? *(B.Com., Panjab)*
2. What are the provisions of law regarding the clubbing of income of spouse and other family members in the income of individual ?
3. Write notes on:
   (*a*) Share of income from A.O.P. firm,
   (*b*) Deemed incomes.

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8 SET-OFF AND CARRY FORWARD OF LOSSES

Set-off loss within head—Speculation loss—Outside head—Carry Forward of losses—Capital losses of firms—Losses of companies—Return of Loss—Chart—Illustrations—Questions.

Income-tax is levied on the total income of any assessee of a previous year. Total income is calculated by aggregating the income of the assessee under different sources of income falling under one head of income and then all the heads of income are put together to find out the net result in the shape of total income. For example, If an assessee is running 3 different types of businesses, *e.g.*, cloth shop business, cycle manufacturing and hosiery goods manufacturing. The income of all the three different businesses is to be aggregated to know the income under the head 'Profits and gains of business or profession'. It is not necessary that every source shall result into a profit every year. There may be loss under one source and profit under other two sources. So when the income of different sources is put together the loss of one source is to be adjusted against the income of other two sources. It, therefore, follows that where the net result in respect of any source is a negative figure, it can be set-off against a positive figure in respect of another source of income under the same head of income. Similarly, when the income of all heads is aggregated, the loss under one head is set-off against the income of another head and if at all the total result is a loss, the same is carried forward over future years for setting off. Sections 70-79 of Income-tax Act deal with the provisions regarding set-off and carry-forward and set-off losses. All these provisions are discussed in the following pages.

SET-OFF LOSSES

Set-off loss from one source against income from another source within the same head of income

The income under one head is computed by adding together the incomes from different sources which fall under the same head. Section 70 says that the loss of one source is adjusted against the income of another source falling under the same head of income. Suppose the assessee is running two-three different businesses and the income of the head is calculated by combining different sources. So it is automatic that if there is loss under one source, the same is adjusted or set-off against the available income under other sources in the same head of income. The loss on sale of stock-in-trade or a current asset is always of revenue nature. Whether a particular transaction causing loss is related to stock-in-trade or current asset is a question of

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law *[Ramnarain Sons Pvt. Ltd. vs. C.I.T. (1961) 41 I.T.R. 534 (SC.)]* but onus to prove that particular asset was held by him as stock-in-trade lies on assessee. *[Bhikam Chand Bagri vs. C.I.T. (1962) 44 I.T.R. 746(Cal.)].*

The shares, which an underwriter has to purchase and which he intends to sell as soon as he can, shall constitute stock-in-trade and any loss on such asset shall be treated as business loss.

There are three *exceptions* to this rule that a loss can be set-off against any other income under the same head:

(i) Speculation loss [Section 73(1)]

Any loss computed in respect of speculation business carried on by assessee shall not be set-off except against profits and gains, if any, of another speculation business.

(ii) Losses from capital assets [Section 70(2)]

(iii) Loss from maintenance of horses [Section 74A(3)]

In case assessee maintains horses for race purpose, he can deduct expenses incurred on such activity out of any income from race course winnings and not from any other income under the head 'Other Sources'.

Set-off of loss from one head against the income of another head in the same Assessment Year [Inter-head setting off losses] [Section 71]

Where in respect of any assessment year, the net result of the computation under any head of income is a loss, the assessee shall, subject to the provisions of this Chapter, be entitled to have the amount of such loss set-off against his income, if any, assessable for that assessment year under any other head. This rule is not applicable to losses under the head *"Capital Gains"*. Loss from any other head can be set-off from capital gain but loss under the head capital gains cannot be set-off from income under any other head.

Loss under the Head "House Property"

Loss under the head "House Property", whether it relates to self occupied or let house property can be set off from any other income of the year. It cannot be carried forward.

Illustration 1. The following are the particulars of income and loss of an individual under different heads of income. Set-off losses in the assessment year 1997-98 and find out the net result:

	Rs.
Income from house property A	5,000
Loss from house property B	– 8,000
Income from interest on securities	20,000
Loss from a cycle business	– 20,000
Profit from speculation business	20,000
Loss from short-term capital asset	– 6,000
Long-term capital loss	– 25,000
Long-term capital gain (Investments)	21,000

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Solution

House property Income:		Rs.	Rs.
Income from house property A		5,000	
Loss from house property B		– 8,000	
Can be set-off			(–) 3,000
Business Income:			
Profit from speculation business		20,000	
Loss from cycle business		– 20,000	
			Nil
Capital Gains:			
(*i*) Long-term capital gains		+ 21,000	
(*ii*) Loss from another long-term Capital asset	(–) 25,000		
(*iii*) Short-term capital loss	(–) 6,000	(–) 31,000	
Unadjusted Capital loss to be C/F		(–) 10,000	Nil
Income from other Sources :			
Interest on securities			20,000
Gross Total Income			17,000

CARRY FORWARD AND SET-OFF LOSS

Where in any assessment year, the loss under any head (except salaries and income from house property) is not adjusted as per rules, the same shall be carried forward and set-off against the income of subsequent years.

(*i*) **Loss under the head "House Property"** No loss under the head income from House Property can be carried forward with effect from assessment year 1997-98.

(*ii*) **Business Loss** [Section 72 (1)]. As explained earlier, the loss under business head except speculation loss, shall be adjusted against the income from any other head in the same assessment year. If the whole business loss cannot be set-off because of insufficiency of income under other heads in the same assessment year, such business loss shall be carried forward and set-off against the income of any business or profession carried on by the assessee and assessable in that assessment year. Thus a business loss can be carried forward over 8 subsequent assessment years and set-off wherever profits are available provided the *same business is continued for which the loss was originally computed.* A carried forward non-speculation business loss can be set-off against the income of any business (including speculation business profit) carried on by the assessee.

The other important points to be noted in the carry forward and set-off business loss, are given as follows:

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(1) The person who has incurred the loss, alone has the right to carry it forward. The successor except succession by inheritance (business passing from father to son) cannot claim to carry forward the loss incurred by his predecessor in business. Where a company merges with another under the scheme of amalgamation, the past loss of the amalgamating company can be carried forward by the new company.

(2) The business loss which can be carried forward must have been computed by the Assessing Officer on the basis of return filed by the assessee under Section 139.

(3) The unabsorbed business loss of an industrial undertaking which was discontinued due to natural calamities (as discussed u/s 33B), shall be carried forward and set-off against the profit of the reconstructed, re-establised business upto a period of 8 years as reckoned from the previous year in which the business is re-started.

(4) Loss of discontinued business can be set-off upto the year in which business is discontinued. The unadjusted loss (whether current or brought forward) of discontinued business cannot be adjusted after the year in which business has been discontinued.

(5) Loss from any asset held as stock-in-trade can be set-off from any income from such asset even if it is taxable under the head 'Other Sources'.

(6) Unabsorbed depreciation can be carried forward for a period of 8 succeeding previous years to be set-off only from the income under the head Profits and Gains of business or profession and not from any income under any other head. The special treatment being given to unabsorbed depreciation upto assessment year 1996-97 has been withdrawn.

(*iii*) **Loss of speculation business.** Where for any assessment year the loss under speculation business has not been wholly set-off against the income of another speculation business, such part of speculation loss shall be carried forward to the following assessment year and set-off only against the profits of any speculation business carried on by the assessee and assessable during those assessment years. The unabsorbed speculation business loss is eligible for carry forward upto eight assessment years immediately succeeding the assessment year for which the loss was computed.

If the assessee leaves one type of speculation business and its unabsorbed loss could not be set-off against the income of any other speculation business which the assessee may start, the carry forward loss of speculation business which is discontinued, is eligible for setting off against the assessee's income of another speculation business.

(*iv*) **Loss under the head "Capital Gains"** (Sec.74). With effect from 1-4-88, *i.e.*, assessment year 1988-89 the capital losses shall be carried forward and set-off in following manner:

(*a*) In case there is capital loss in a previous year and it cannot be set-off from any other income of the year, the unabsorbed portion, if any, shall be carried forward to the following assessment year to be set-off only from Capital Gains, if any. If still unadjusted it can be carried forward to succeeding previous year and so on. [Section 74 (1)]

(*b*) No loss under the head Capital Gain shall be carried forward for more than 8 assessment years succeeding the assessment year in which such loss was first computed. [Section 74 (2)]

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(*c*) The old provisions of set-off and carry forward of short-term and long-term capital loss continue to remain in operation for the capital losses in respect of assessment year 1987-88 and earlier assessment years but subject to following deduction:

A. if the capital loss of earlier years relates to short-term capital asset it shall be carried forward as per section 74(1) and 74(2) above.

B. if the capital loss of earlier years relates to long-term capital asset, it shall be reduced by the amount of deduction u/s 48(3) and balance, if any, shall be adjusted from the capital gain of the year and if still unadjusted shall be further C/F to succeeding previous year but such carry forward shall not be allowed beyond the fourth assessment year immediately succeeding the assessment year for which the loss was first computed. [Section 74 (3)]

(*v*) **Loss under the head 'Other Sources'** [Section 74A (3)]. Under the head *'Other Sources'* only expenses on maintenance of horses can be set-off from race winnings if any. If it still remains unadjusted, it can be carried forward for 4 succeeding previous years to be set-off from income of such activity or race winnings.

Losses of Firms

[Section 75]—In case of firm assessed as firm any loss relating to assessment year prior to 1993-94, which was apportioned amongst partners and partners could not adjust it from income of assessment year 1992-93, such loss shall be set-off and carried forward as per provisions of section 70, 71, 72, 73, 74 and 74A to be set-off only from income of the firm assessed as firm.

Losses in case of change in constitution of a firm [Section 78]

Where a change has occurred in the constitution of a firm, nothing shall entitle the firm to have carried forward and set-off so much of the loss proportionate to the share of a retired or deceased partner as exceed his share of profits, if any, in the firm in respect of that previous year.

Set-off of Current and Brought Forward Losses

Where in respect of an assessment year, there is income under a head, the loss, if any, under any other head for that assessment year should first be set-off against it before the carried forward losses under the former head can be set-off against such income. (Circular No. 587 dated 11-12-1990).

The above clarification simply means that current loss from any other head will have precedence over brought forward loss of the same head.

Illustration 2. Compute taxable income and loss to be C/F:

	Rs.
(*i*) Business profit for the previous year 1996-97	20,000
(*ii*) B/F Business Loss of 1994-95	10,000
(*iii*) Capital loss on shares	60,000
(*iv*) Loss from self-occupied house (u/s 23(2)]	5,000

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Solution

Adjustment of Losses during Assessment year 1997-98

		Rs.
House Property:	Loss from self-occupied house (u/s 23(2)]	(–) 5,000
Profits & Gains:	Business Profit	(+) 20,000
	Available income	(+) 15,000
	B/F Business Loss of 1994-95	(–) 10,000
	Total Income	(+) 5000
Capital Gain :	Capital loss to be C/F	60,000

Losses in Case of Succession of Business or Profession

Sec. 78(2) says that where any person carrying on any business or profession has been succeeded in such capacity by another person otherwise than by inheritance, that another person shall not be entitled to carry forward and set-off the losses incurred by his predecessor against the profits earned by him after succession. In case of inheritance, the heir would be entitled to carry forward the loss incurred by the previous owner *i.e.*, the predecessor. The successor in business is normally treated as if he had commenced a new business.

Provisions relating to carry forward and set-off accumulated loss and unabsorbed depreciation in certain cases of amalgamation [Section 72 (A)]

In case a company owning an industrial undertaking amalgamates with another company, the accumulated loss and the unabsorbed depreciation of amalgamating company shall be deemed to be the loss or depreciation of the amalgamated company for the previous year in which amalgamation was effected and the other provisions of this Act relating to set-off and carry forward of loss and unabsorbed depreciation shall apply accordingly provided the following conditions are fulfilled:

(*i*) that the accumulated loss of the amalgamating company before amalgamation exceeds fifty per cent of the aggregate of its paid-up share capital;

(*ii*) that the amalgamating company was not, immediately before its amalgamation, financially viable;

(*iii*) that amalgamation was in public interest;

(*iv*) that such other conditions as Central Government may notify in the Official Gazette to ensure that the benefit under this section would facilitate the rehabilitation; or revival of the business of amalgamating company; and

(*v*) the Central Government makes declaration to this effect [Section 73A(1)].

The benefit to set-off or carry forward shall not be available to the amalgamated company if it carries on the business of amalgamating company after making any

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modification or reorganisation and such modification or reorganisation are not approved by prescribed authority. The amalgamated company shall have to furnish, alongwith return of income, a certificate from the specified authority to the effect that adequate steps have been taken by the company for the rehabilitation or revival of the business of the amalgamating company [Section 72(2)].

The Finance Act, 1987 has introduced sub-section (3) under which specified authority shall communicate to the amalgamating company about the fact that it is satisfied with the scheme submitted and it would make such recommendations to the Central Government after amalgamation is affected.

Accumulated Loss. Means so much of loss of the amalgamating company under the head "profits and grains of business or profession" (not being a loss sustained in a speculation business) which the amalgamating company would have been entitled to carry forward and set-off under the provisions of section 75, if the amalgamation had not been affected.

Unabsorbed Depreciation. Means so much of the allowance of depreciation of the amalgamating company which remains to be allowed and which would have been allowed to the amalgamating company under the provision of the Act if the amalgamation had not been affected.

Carry forward and Set-off Lossess of Certain Companies [Section 79]

Where change in shareholding has taken place in a previous year in the case of a company not being a company in which the public are substantially interested, no loss incurred in any year prior to the previous year shall be carried forward and set-off against the income of the previous year unless:

On the last day of the previous year the shares of the company carrying not less than 51% of the voting power were beneficially held by person who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred.

In case change in voting power takes place in a previous year due to death of a shareholder or on account of transfer of shares by way of gift to any relative, the above-mentioned provision shall not be applicable.

Filing of Return of Loss [Sec. 139]

For any loss to be carried forward and set-off against the income of a subsequent year the return of such loss must be filed under Sec. 139 and the I.T.O must determine the loss on the basis of the return filed. Only such loss is eligible for carry forward which was determined by the I.T.O. on the basis of return filed by the assessee and after determining the loss, the I.T.O. should have informed or notified the loss to the assessee. On the basis of this explanation, the conclusion can be that if no return is filed for the year in which the loss was incurred, the right to carry forward the loss would be lost.

Order in which current and brought forward losses are to be adjusted

In case different types of allowances and losses of current and that of past years are accumulated, the following order is to be observed. It means, if in any year

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past losses, unabsorbed depreciation, current depreciation, unabsorbed investment allowance etc., are to be allowed against the current business profits, the order to be followed is given as follows:

Out of profits of the current previous year the losses and expenses will be adjusted in following order :—

1. Current expenditure on scientific research whether capital or revenue;
2. Current depreciation of the year;
3. Current loss of another business;
4. Brought forward business losses of earlier years (oldest loss to be adjusted first) and B/F unabsorbed depreciation;
5. Brought forward expenditure on promotion of family planning (only in case of companies);
7. Brought forward unabsorbed expenditure on scientific research;
8. Brought forward Development Allowance;
9. Brought forward Investment Allowance.

CHART SHOWING SET-OFF AND CARRY FORWARD AND SET-OFF OF LOSSES

Loss	*Adjustment*
1. Within the Head	(*i*) Loss from one source of income can be set-off from income of another source except speculation loss and losses under section 56(2) (*iii*) (Expenses on-maintenance of horses).
	(*ii*) Speculation loss can be set-off from speculation gain, if any. But loss from any other source can be set-off from speculation gain, if any.
	(*iii*) Losses under section 56(2) (*iii*) *i.e.*, expenses on horses for race purposes can be set-off only from race course winnings and not from any other income.
2. Outside Head	(*i*) Loss from one head of income can be set-off against income of another head except (*a*) Speculation loss,,
	(*b*) Casual losses (both of them explained above),
	(*c*) Unrealised rent under 'House property',
	(*ii*) Loss from house property can be set-off from any other head.
	(*iii*) Unrealised rent from house property can be set-off only from income of another house property, but not from any other income.
3. Capital Loss	(*i*) Capital losses can be set-off from (*a*) short-term capital gain, (*b*) long-term capital gain. Loss from any other head of income can be set-off from capital gain, if any.
Carry-Forward and Set-off	
	Carrying the loss of one previous year to following previous year and adjusting it. There can be no loss under the head 'Salaries'.
1. House Property	No loss under this head can be C/F.

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Loss	*Adjustment*
2. Business Loss and unabsorbed depreciation	Can be carried forward for 8 previous years succeeding the relevant previous years to be set-off from any business income provided the business whose loss is being carried forward continues. Loss of discontinued business cannot be carried forward.
3. Speculation Loss	Can be carried forward for 8 succeeding previous years to be set-off only from speculation gain, if any, during any of the 8 previous years.
4. Capital Loss	Can be carried forward for 8 previous years succeeding the relevant previous year to be set-off ONLY from capital gain, if any
5. Expenses incurred on maintenance of horses for race purposes	Can be carried forward for 4 succeeding previous years to be set-off only from race course winnings, if any. Loss from horse races cannot be carried forward.

Illustration 3. The following are the particulars of income/loss of Mr. A. You are required to set-off losses and carry forward and set-off where necessary.

	Assessment year 1996-97	*Assessment year 1997-98*
	Rs.	Rs.
Income from salary (computed)	15,000	15,000
Income from Interest on Securities (Gross)	5,000	5,000
Loss from business	53,000	15,000
Short-term capital gain	8,000	—
Long-term capital gain (Land)	21,000	—

Solution

	Rs.	Rs.
Assessment year 1996-97		
Salary Income (Computed)		+ 15,000
Business Loss		– 53,000
Capital Gain: Short-term	8,000	
Long-term	21,000	
		+ 29,000
Other Sources: Interest on Securities		+ 5,000
Gross Total Income		+ Nil

Note: Business loss of Rs. 53,000 shall be adjusted against income of all other heads and business loss to be C/F Rs. 4.000.

Assessment year 1997-98	Rs.	Rs.
Salary Income (Computed)		15,000
Business Loss		– 15,000
Other Sources: Interest on Securities		5,000
Gross Total Income		5,000

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Note: Business loss B/F from assessment year 1996-97 cannot be set-off as assessee has no income under the head Profits and Gains of Business or Profession. Hence he can C/F loss of assessment year 1996-97. *i.e.*, Rs. 4,000.

Illustration 4. From the following particulars of income of assessees A, B and C, how the capital losses shall be set-off and carried forward for the previous year ending on 31-3-1997 ?

			Rs.
(A)	(*i*)	Business income	15,000
	(*ii*)	Short-term capital loss	1,200
	(*iii*)	Long-term capital gain (shares)	7,200
(B)	(*i*)	Business income	30,000
	(*ii*)	Short-term capital loss	40,000
(C)	(*i*)	Business income	60,000
	(*ii*)	Short-term capital gain	20,000
	(*iii*)	Long-term capital gain (land)	17,000
	(*iv*)	Carry forward loss (short-term capital assets)	50,000

Solution

			Rs.	Rs.
(A)	(*i*)	Business income		15,000
	(*ii*)	Long-term capital gain (shares)	7,200	
		Less : Short-term capital loss	1,200	
		Net capital gain		6,000
		Gross Total Income		21,000
(B)	(*i*)	Business Income		30,000
	(*ii*)	Short-term capital loss to be C/F Rs. 40,000		—
		Gross Total Income		30,000
(C)	(*i*)	Business income		60,000
	(*ii*)	Long-term capital gain (Land)	17,000	
	(*iii*)	Short-term capital gain	20,000	
			37,000	
		Set-off Short-term capital loss B/F	50,000	
		Capital loss still to be C/F	13,000	
		G.T.I.		Nil
				60,000

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Illustration 5. Mr. Atul, an Indian resident, furnishes the following particulars of his income for the assessment year 1997-98. You are required to deal with set-off and carry forward of losses.

	Rs.
(*i*) Income from securities (Gross)	10,000
(*ii*) Income from residential house (computed)	5,000
(*iii*) Profits from Rayon business	25,000
(*iv*) Income from an agency business	2,000
(*v*) Speculation income	2,000
(*vi*) Short-term capital gain	4,000
(*vii*) Long-term capital gain	9,500
The carry forward items from the assessment year 1996-97 are:	
(*i*) Loss from Hosiery Business (discontinued)	4,000
(*ii*) Loss in agency business	3,000
(*iii*) Loss from Rayon business	3,000
(*iv*) Speculation loss	4,000
(*v*) Short-term capital loss	6,000
(*vi*) Long-term capital loss [of previous year 1993-94]	6,500

Current year's depreciation for rayon business is Rs. 500

Solution

Computation of Gross Total Income

		Rs.	Rs.
(1) Income from House Property			+5,000
(2) Business income:			
(*i*) *Speculation Business:*			
Income from speculation business		+2,000	
Set-off brought forward speculation loss		–4,000	
Carry-forward speculation loss		–2,000	
(*ii*) *Rayon Business:*			
Income from Rayon business		25,000	
Less: Current depreciation		500	
		24,500	
Set-off brought forward business loss of Rayon business		3,000	
		21,500	
(*iii*) Income from agency business	(+) 2,000		
Set-off Loss B/F	(–) 3,000		
		(–)1,000	
			20,500

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(3) Capital Gains:			
Short-Term Capital Gain		4,000	
Long-Term Capital Gain		9,500	
Total Capital Gain		13,500	
Set-off B/F capital loss			
S.T.C. Loss	6,000		
L.T.C. Loss	6,500		
		12,500	
Net Capital Gain			1,000
(4) Other Sources: Interest on Securities			10,000
Gross Total Income			36,500

Note: (*i*) Loss of a discontinued business cannot be set-off against the income of a continued business.

(*ii*) Speculation business loss will be carried forward because the speculation loss cannot be set-off against non-speculation business income.

Illustration 6. The following are the particulars of income of an assessee as determined by the I.T.O for the assessment year 1997-98. Compute his total income.

Assessment Year 1996-97	Rs.
Silver speculation loss (Discontinued)	10,000
Hosiery business loss	6,000
Rolling Steel Mill profit (before charging of depreciation of Rs. 10,000)	8,000
Profit from another business	5,000
Income from house property	2,000
Assessment year 1997-98	
Gold speculation profit	20,000
Hosiery business loss	2,000
Rolling Steel Mill profit (before charging depreciation of Rs. 10,000)	6,000
Profit from another business	16,000
Income from house property	2,000

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Solution

Computation of total income of an assessee

Assessment Year 1996-97	Rs.	Rs.
(1) Income from house property		+ 2,000
(2) (*i*) *Business profit*		
Rolling Steel Mill profit	8,000	
Less: Depreciation	– 10,000	
Unabsorbed depreciation is	– 2,000	
(*ii*) Income from another business	+ 5,000	
(*iii*) Hosiery business	(–) 6,000	
(Set it off against other income)		– 1,000
(*iv*) Silver speculation loss to be C/F 10,000		Nil
Available Income		+ 1,000
Set-off unabsorbed depreciation upto available income		–1,000
Gross Total Income		Nil

Unabsorbed depreciation of Rs. 1,000 and speculation loss of Rs. 10,000 are to be carried forward.

Assessment Year 1997-98		Rs.	Rs.
1. Income from House Property			2,000
2. *Profit and Gains*			
(*i*) Rolling Steel Mill		+ 6,000	
Depreciation		(–) 10,000	
Unabsorbed depreciation		(–) 4,000	
(*ii*) Income from another business		+ 16,000	
(*iii*) Speculation Gain	Rs. 20,000		
Set-off B/F speculation Loss	Rs. 10,000		
		+10,000	
		22,000	
Less: Current Hosiery Business Loss		(–) 2,000	
		20,000	
Less: B/F Depreciation		(–) 1,000	
			19,000
Gross Total Income			21,000

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Illustration. 7. From the following particulars, determine assessable profit or loss to be carried forward as the case may be for the assessment year 1997-98

		Rs.
1.	Loss for 1989-90 carried forward	1,00,000
2.	Loss for 1990-91 carried forward	15,000
	Depreciation allowance for 1990-91 carried forward	5,000
3.	Loss for 1991-92 carried forward	10,000
	Depreciation allowance for 1991-92 carried forward	5,000
4.	Loss for 1992-93 carried forward	5,000
	Depreciation Allowance for 1992-93 C/F	2,500
5.	Loss for 1993-94 carried forward	5,000
	Depreciation allowance for 1993-94 carried forward	2,500
6.	Profit for 1994-95	15,000
	Depreciation due for 1994-95	5,000
7.	Profit for 1995-96	50,000
	Depreciation due for 1995-96	10,000
8.	Profit for 1996-97	1,20,000
	Depreciation due for 1996-97	10,000

Solution

Determination of Assessable Profits

1. *For the previous year 1994-95*

	Rs.	Rs.
Profit		15,000
Less: Current depreciation	5,000	
Less: B/F loss from 1989-90	10,000	
		15,000
		Nil

Rs. 90,000 loss of 1989-90 to be carried forward. All other losses will also be carried forward.

2. *For the previous year 1995-96*

	Rs.	Rs.
Profit		50,000
Less: Current depreciation	10,000	
Less: B/F loss from 1989-90	40,000	
		50,000
		Nil

Rs. 50,000 Loss of 1989-90 and all other losses to be carried forward.

3. *For the previous year 1996-97*

		Rs.
Profit		1,20,000
Less: Depreciation for 1996-97	10,000	
B/F Loss for 1989-90	50,000	
B/F Loss for 1990-91	15,000	
B/F Loss for 1991-92	10,000	
B/F Loss for 1992-93	5,000	
B/F Loss for 1993-94	5,000	

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Unabsorbed depreciation for 1990-91	5,000	
Unabsorbed depreciation for 1991-92	5,000	
Unabsorbed depreciation for 1992-93	2,500	
Unabsorbed depreciation for 1993-94	2,500	
		1,10,000
Gross Total Income		10,000

Illustration 8. Mr. Deepak Jain, who is carrying on the business of dealing in shares and securities, agencies and trading in garments. He submits the following particulars about his business :

	Assessment years			
Business	*1994-95* Rs.	*1995-96* Rs.	*1996-97* Rs.	*1997-98* Rs.
Share dealing	(–) 1,00,000 C/F	(–) 60,000 C/F	(–) 20,000 C/F	+ 2,40,000
Securities dealing	—	—	(–) 1,00,000	+ 40,000
Agency (discontinued from 1-6-96)	(–) 20,000 C/F	(–) 30,000 C/F	(–) 1,00,000 C/F	(–) 10,000
Interest on securities (held as stock-in-trade)	—	—	—	+ 20,000
Garment dealing	—	—	—	+ 1,00,000

Loss of Agency business relating to assessment year 1988-89 which still remains to be adjusted is Rs. 45,000.

Compute his total income for the assessment year 1997-98.

Solution

Computation of total income for the assessment year 1997-98

Profits and gains of Business or Profession		Rs.
Profits from	(*i*) Share business	2,40,000
	(*ii*) Security dealing	40,000
	(*iii*) Garment dealing	1,00,000
		3,80,000
Adjust current loss from agency business		10,000
		3,70,000

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Adjust brought forward losses

	Rs.	
Assessment year 1994-95		
Loss from (*i*) Share dealing	1,00,000	
(*ii*) Agency	20,000	
		1,20,000
		2,50,000
Assessment year 1995-96		
Loss from (*i*) Share dealing	60,000	
(*ii*) Agency	30,000	
		90,000
		1,60,000
Assessment year 1996-97		
Loss from (*i*) Share dealing	20,000	
(*ii*) Agency	1,00,000	
(*iii*) Security	1,00,000	
		2,20,000
Balance loss to be adjusted from income under the head "Other Sources" out of interest on securities held as stock-in-trade		60,000
Income from other sources		
Interest on securities held as stock-in-trade		20,000
Business loss b/d to be adjusted from this income		(–) 60,000
Business loss to be carried forward		40,000

Note : Loss of discontinued business can be adjusted upto the year in which business is discontinued.

Q. No. 1

From the particulars given below, compute the total income for the previous year 1996-97.

	Rs.
(*i*) Income from Let-out house (computed)	6,000
(*ii*) Annual Rental value of his self-occupied house	4,000
(*iii*) Municipal Taxes	400
(*iv*) Profit from electric goods business after depreciation	10,000
(*v*) Profit from agency business	3,000
(*vi*) Speculation gain from Gold	2,000
(*vii*) Long-term Capital Gain from shares	7,000
(*viii*) Short-term Capital Gain	2,000
Following losses have been brought forward from 1995-96 previous year:	
(*i*) Loss from electric goods business	6,000
(*ii*) Loss from an agency business	1,000
(*iii*) Speculation loss from silver	4,000
(*iv*) Unabsorbed Dep.	12,000

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(*v*) Long-term capital loss (shares)	4,400
(*vi*) Short-term capital loss	3,000

[**Hints:** House Property: Let-out Rs. 6,000; Self-occupied Exempted; Business income Rs. 5,000; Capital Gain Rs. 1,600; Total income Rs. 12,600. Speculation unabsorbed loss Rs. 2,000 C/F] [P-7]

Q. No. 2

Mr. Singh, a resident of India, submits the following particulars of his income for the assessment year 1997-98:

	Rs.
(*i*) Income from house let out (computed)	9,500
(*ii*) Profit from radio business	19,600
(*iii*) Profit from Electric business	1,800
(*iv*) Speculation Income	1,900
(*v*) Short-term capital gains	3,200
(*vi*) Long-term capital gains (Gold)	9,250

Current year's depreciation relating to electric goods business is Rs. 2,500.

The following items have been brought forward from proceeding assessment year.

	Rs.
(*i*) Loss from cycle business discontinued during the previous year 1995-96	3,900
(*ii*) Loss from electric business	2,700
(*iii*) Loss from radio business	1,900
(*iv*) Unabsorbed depreciation of electric business	1,000
(*v*) Unabsorbed family planning expenditure	2,600
(*vi*) Speculation loss	3,200
(*vii*) Short-term capital loss from the year 1993-94	4,100
(*viii*) Long-term capital loss from the year 1992-93	6,450

You are required to compute his gross total income and deal with the carry forward of losses. *(M. Com. B.H.U.)*

[**Hints:** Income from House Property Rs. 9,500; Unabsorbed exp. on family planning cannot be set-off, Loss from discontinued cycle business cannot be set-off, Business Profit after setting-off loss from radio business, loss of firm, unabsorbed depreciation, Rs. 13,300; Speculation loss of Rs. 1,300 to be C/F, Capital Gains Rs. 12,450; Set-off of capital losses Rs. 10,550; Taxable Capital Gain Rs. 1,900; Total Income Rs. 24,700] [P-3].

Q. No. 3

Mr. Ram Patel submits the following informations of his incomes and losses for the year ending 31-3-97 :

	Rs.
(1) Salary income (computed)	24,000
(2) Income from house property :	
House A (income)	10,000
House B (loss)	30,000
House C (self-occupied) loss	8,000
(3) Income from business :	
Cloth business (profit)	10,000
Hardware business (loss)	12,000

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	Speculation (profit)	12,000
	Speculation (loss)	17,000
(4)	Capital gains :	
	Short-term (gain)	8,000
	Short-term (loss)	24,000
	Long-term (gain)	8,000
(5)	Other Sources :	
	Income from betting	12,000
	Loss from card games	6,000
	Income from card games	9,000
	Interest on securities (gross)	8,000

(B.Com. Mangalore)

[**Hints:** Loss from HP Rs. 28,000 and Business loss of Rs. 2,000 to be adjusted from other heads. Speculation loss to be C/F Rs. 5,000. Capital loss to be C/F Rs. 8,000. Other Sources Income Rs. 24,000, Loss from card games cannot be set-off from income from card games. Total Income Rs. 18,000]

Q. No. 4

The assessment of M Co. Ltd., Indian Company, for the years 1996-97 and 1997-98 show the following results:

	Ass. year 1996-97	Ass. year 1997-98
(*i*) Interest on securities	(–)2,000	+2,000
(*ii*) Income from House Property	+8,000	+8,000
(*iii*) Profit and Gains of Business or Profession		
(*a*) dealing in fruits	–30,000	–12,000
(*b*) manufacturing glass:		
Profit before depreciation	+50,000	+1,40,000
Depreciation	80,000	75,000
(*c*) Speculative transactions	+6,000	–9,000
(*iv*) Income from other Sources: Bank Interest	+2,000	+5,000
(*v*) Short-term Capital Gains	Nil	–25,000

Compute the net assessable results for each of the two years giving full reasons for your workings.

(C.U. M.Com.)

[**Hints:** *Assessment year 1996-97.* Income Nil, Glass Business Profit Rs. 50,000. Current depreciation adjusted Rs. 50,000, C/F Rs. 30,000 Fruit dealing business loss adjusted upto Rs. 6,000 from speculation Gain, Rs. 8,000 from Income of all other heads C/F Rs. 16,000.

Assessment year 1997-98. H.P. Income Rs. 8,000 profits and gain Rs. 7,000 capital loss Rs. 25,000 to be carried forward. Other source Rs. 7,000 Total Income Rs. 22,000. Speculation loss to be carried forward Rs. 9,000 [P-8].

Q. No. 5

T, a partner of a PFAF and also having several sources of income, furnishes the following particulars in respect of his assessment for the year 1997-98 :—

	Profit / Loss
(*i*) Income from house property	+ Rs. 6,000
(*ii*) Interest on securities	+ Rs. 2,000

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(*iii*) Profit & gains of business or profession:	
Business A : Trading profits	+ Rs. 10,000
Depreciation	Rs. 6,000
Business B : Trading profits	Rs. 50,000
Depreciation	Rs. 12,000
(*iv*) Income from other sources :	
Dividends (Gross)	+ Rs. 2,000
Interest on loan taken by T for purchase of shares on which the dividend was earned	Rs. 600
(*v*) Capital Gains :	
Short-term capital gains	Rs. 12,000

It is found that unabsorbed depreciation relating to Business B, amounting to Rs. 15,000 as brought forward from the assessment year 1994-95. From Business A, unabsorbed loss of Rs. 20,000 is brought forward from the assessment year 1994-95.

Compute the total income of T for assessment year 1997-98.

[C.U., M.Com.]

[**Hints :** Profits and Gains Rs. 7,000 Capital Gains Rs. 12,000 Other Sources Rs. 3,400; Deduction u/s 80 L Rs. 1,400 Total Income Rs. 27,000] [P-5]

Q. No. 6

The particulars of assessment years 1996-97 and 1997-98 are as under :—

	1996-97 Rs.	1997-98 Rs.
Income from house property	(+) 8,000	(+) 8,000
Profits and gains from business or profession :		
A. Manufacturing business :		
Trading profit or loss before Depreciation	(–) 15,000	(+) 36,000
Depreciation	32,000	23,000
B. Speculative transactions	(+) 6,000	(–) 8,000
Income from other sources	(+) 5,000	(+) 6,000
Capital gains :		
Short-term loss	NIL	(–) 5,000

Compute the total income for each assessment year.

[Calcutta University, M.Com.]

[**Hints :** *Assessment year 1996-97* Total income NIL unabsorbed dep. to be C/F Rs. 28,000

Assessment year 1997-98 Total income NIL unabsorbed dep. C/F Rs. 1,000; Speculation loss of Rs. 8,000 to the C/F STC loss C/F Rs. 5,000] [P-6]

QUESTIONS

1. Explain the provisions of Income-tax Act, 1961 regarding carry forward and set-off of losses. *(Nagpur M. Com. 1979; Guru Nanak B.Com.)*
2. Are there any special provisions for setting-off losses in respect of speculation business, firms assessed as firm and firm assessed as A.O.P.

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9 Deductions to be Made in Computing Total Income

Gross total income—Definitions—Deductions in respect of certain payments 80D to GGA—Deductions in respect of certain incomes 80HH to 80U—Chart—Illustrations—Questions.

The aggregated income from all the heads of income is known as Gross Total Income.

In computing the total taxable income of an assessee, certain deductions under sections 80D to 80U are allowed from his **Gross Total Income**. It means, firstly, that the income of the assessee shall be calculated under five specific heads of income and incomes from all heads are put together and then from this total, certain deductions are made and after making deductions whatever remains shall be the total income or total taxable income.

The deductions to be allowed from the Gross Total Income are to be distinguished from the deductions which are made while computing income under different heads discussed earlier. The deductions made from the gross total income are either incentives to save for future or a kind of relief to the assessee in certain cases. On the other hand, the deductions made while computing income under different heads are allowed to meet the expenses which are necessary, wholly, totally and exclusively incurred in earning income under these heads of income.

Section 80A(2) says that the aggregated amount of deductions under this chapter, shall not, in any case, exceed the Gross Total Income of the assessee.

Section 80A(3) says that where a deduction has been claimed under sections 80G, 80GGA 80HH 80HHA, 80HHB 80HHC, 80HND, 80HHE and 80IA in computing the total income of an association of persons or a body of individuals, no deduction under the same section shall be allowed in computing the total income of a partner of the firm or a member of the association or body in relation to his share in the income of association or body of individuals.

Before going through these deductions it is advisable to study different definitions of the terms used in this chapter. Section 80B of Income-tax Act deals with these definitions.

Displaced person means a person who, on account of partition of India or, on account of civil disturbance or fear of such disturbance in East Pakistan, left his place of residence in Pakistan and who has been subsequently residing in India.

U/s 80B (5) *Gross Total Income* means the total income computed in accordance with the provisions of this Act, before making any deduction under this

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chapter. U/s 112 (2) where the gross total income of an assessee includes any income arising from the transfer of long term capital asset, the gross total income shall be reduced by the amount of such income and balance income shall qualify for deduction u/s 80. This means this gross total income is the figure which is arrived at after computing income under various heads, adjusting the losses of the current year, brought forward losses from earlier years and after including the income of other persons to be included in the income of assessee.

Priority Industry [80B (7)] means the business of generation or distribution of electricity or any other form of power, or construction, manufacture or production of any one or more of the articles or things specified in the list in the Sixth Schedule or the business of any hotel where such business is carried on by an Indian Company and the hotel is for the time being approved in this behalf by the Central Government.

Repatriare according to section 80B (9), means a person of Indian origin who was ordinarily residing in a foreign country and who, on leaving or being forced to leave such country, has returned to India with the intention of permanently residing therein. The following are the cases of repatriation:

(*a*) in case of a person leaving Mozambique, on or after the 25th day of June 1962; or

(*b*) in case of a person leaving Burma, on or after the 1st day of June 1963; or

(*c*) in case of a person leaving Ceylon, on or after the 1st day of November 1964; or

(*d*) in case of a person leaving any other country, on or after such date or dates as may be notified in this behalf by the Central Government in the Official Gazette.

A person is deemed to be of Indian origin if he or either of his parents or any of his grand-parents was born in undivided India.

Deductions

These deductions are divided under two categories:

A. Deductions in respect of certain payments.

B. Deductions in respect of certain incomes.

DEDUCTIONS IN RESPECT OF CERTAIN PAYMENTS

1. Deduction in respect of contribution to Pension Fund [Section 80CCC]

(*i*) This deduction is allowed to individuals only.

(*ii*) This deduction is allowed if certain amount is paid during relevent previous year to Life Insurance Corporation to effect a contract of annuity or pension out of a fund set up u/s 10(23AAB).

(*iii*) The rate of deduction is **actual amount** paid under this scheme (excluding any interest or bonus accrued during the year) or **Rs. 10,000 p.a.** whichever is less.

(*iv*) In case any amount is received by assessee or his nominee under this scheme as pension or any amount is withdrawn by surrender of this plan either in full or in part in any previous year, whole of such amount shall become taxable in the year in which such pension is received or withdrawl is made.

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(*v*) The amount on which deduction under this section is claimed shall not qualify for rebate u/s 88.

2. Deduction in respect of Medical Insurance Premia [Section 80D]

With effect from assessment year 1987-88 any insurance premia paid by Individual or H.U.F. by cheque for an insurance on the health of self or any member of family or dependent parents or Rs. 6,000 p.a. whichever is less shall be allowed as deduction. Such insurance should be in accordance with scheme framed by General Insurance Corporation such as *Mediclaim.*

Q. No. 1

Mr. R paid the following insurance premia during the previous year 1996-97. Compute the amount of deduction admissible u/s 80D :—

	Rs.
(*i*) Life Insurance Premium on own life	6,000 p.a.
(*ii*) Premium paid by cheque to General Insurance Corporation to ensure the health of wife and children	3,000 p.a.
(*iii*) Accident Insurance Premium	3,000 p.a.
(*iv*) Premium paid by cheque under Mediclaim to ensure the health of dependent mother	2,000 p.a.
(*v*) Premium paid to G.I.C. under Mediclaim in cash to ensure own health	3,000 p.a.

[**Hints** : Deduction u/s 80D for premium paid to ensure the health of wife and mother to qualify *i.e.* Rs. 5,000 to be allowed as deduction. Others not to qualify]

3. Deduction in respect of medically handicapped dependents [Section 80DD]

In case an individual or H.U.F. has during the relevant previous year incurred any expenditure for the medical treatment (including nursing), training and rehabilitation of a person who—

(*a*) is a relative of the individual or is a member of H.U.F. and is dependent upon such-individual or H.U.F. and

(*b*) is suffering from a permanent physical disability or mental retardation which is certified by a doctor, surgeon, oculist or a psychiatrist working on a Government hospital, and

(*c*) such disability has the effect of reducing considerably the capacity of such person for normal work or engaging in gainful employment—

a deduction of Rs. 15,000 shall be allowed.

For the purposes of section 80DD—

(*i*) Permanent physical disability shall be regarded as a permanent physical disability if it falls in any one of the categories specified below, namely:

(*a*) permanent physical disability of more than 50 per cent in one limb; or

(*b*) permanent physical disability of more than 60 per cent in one or more limbs; or

(*c*) permanent and total loss of voice;

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(*ii*) blindness shall be regarded as a permanent physical disability, if it is incurable and falls in any one of the categories specified below, namely:

All with corrections

	Better eye	*Worse eye*
(*a*)	6/60-4/60 or Field of vision 110-20	3/60 to Nil
(*b*)	3/60 to 1/60 or Field of vision 100	F.C. at 1 foot to Nil
(*c*)	F.C. at 1 foot to Nil or Field of vision 100	F.C. at 1 foot to Nil or Field of vision 100
(*d*)	total absence of sight	total absence of sight;

(*iii*) mental retardation shall be regarded as mental retardation if intelligence quotient is less than 50 on a test with a mean of 100 and a standard deviation of 15 such as the Wechsle scale."

[Notification No. 142/24/90 TDL No. 8986 Dt. 27.1.92]

Q. No. 2
Mr. D is karta of an H.U.F. The H.U.F. has a child (son of D's brother) who is mentally retarded. Mr. D's mother is also physically disabled. The H.U.F. has spent Rs. 24,000 on their treatment and rehabilitation. Can H.U.F. claim deduction u/s 80D and if yes, how much ?
[**Hints :** H.U.F. can claim deduction of Rs. 15,000 only u/s 80DD]

4. Deduction in respect of deposit made for maintenance of handicapped dependent [Section 80 DDA]

(*i*) This deduction is allowed to individual and H.U.F. only.

(*ii*) The person must be resident of India.

(*iii*) Such individual or H.U.F. has a dependent who is handicapped.

(*iv*) Such individual or H.U.F. makes a deposit with Life Insurance Corporation or Unit Trust of India under a scheme approved by the Central Board of Direct taxes.

(*v*) The scheme must provide for any annuity or lumpsum payment for the benefit of handicapped dependent in the event of death of individual or member of H.U.F.

(*vi*) A deduction of Rs. 20,000 p.a. or actual amount deposited shall be admissible with effect from assessment year 1996-97.

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(*vii*) In case of death of Individual or member of H.U.F., before the death of handicapped dependent, the amount on which deduction was allowed earlier will become taxable.

5. Deduction for expenditure incurred on medical treatment of notified disease or ailment [Section 80DDB]

In case any expenditure is incurred by an individual on his own treatment or on treatment of a dependant relative or in case of HUF on the treatment of any member of HUF and such patient is suffering from disease which is so notified by the CBDT, a deduction of **Rs. 15,000 p.a.** shall be allowed on production of a certificate in prescribed form and from a prescribed authority.

6. Deduction in respect of loan taken for higher education [Section 80 E]

The Finance Act 1994 had introduced the following deduction from 1995-96 :

In case of an individual takes loan from financial institutions or charitable institutions (so approved) for the purpose of pursuing his higher education he shall be entitled to claim a deduction of—

(*i*) Actual Amount of loan repaid alongwith interest on such loan; or

(*ii*) Rs. 25,000 p.a. whichever is less.

This deduction will be allowed for initial assessment year *i.e.* in which repayment of loan starts and seven succeeding assessment years or upto the year in which repayment comes to an end. 'Higher education' means full time study for any graduate or post-graduate course in engineering, medicine, management or post graduate course in applied sciences or pure sciences including maths and statistics.

> **Q. No. 3**
> Mr. Simaranjit Singh left on 1.4.1994 for U.S.A. for his higher studies. For this purpose he had taken a loan from Bank. He started repaying this loan with effect from 1.4.1996 and during 1996-97 he repaid Rs. 20,000 as principal amount and Rs. 8,000 as interest. Can be claim any benefit under Income-tax Act 1961 for the amount repaid by him.
> **[Hints :** Deduction u/s 80E for Rs. 25,000 can be claimed]

7. Deduction in respect of donations to certain Funds, Charitable Institutions etc. [Section 80G]

Section 80G grants partial deduction in respect of amounts given as charitable donations and it is allowed to all assessees.

The sums paid to the following as donations during the previous year qualify under the section:

80G(2): (*a*) any sums paid by the assessee in the previous year as donations to:

(*i*) The National Defence Fund set up by the Central Government; or

(*ii*) The Jawaharlal Nehru Memorial Fund referred to in the Deed of declaration or Trust adopted by the National Committee at its meeting held on the 17th day of August, 1964; or

(*iii*) The Prime Minister's Drought Relief Fund; or

(*iiia*) The Prime Minister's National Relief Fund; or

(*iiiaa*) The Prime Minister's Armenia Earthquake Relief Fund; or

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(*iiiab*) The Africa (Public Contributions) India Fund; or

(*iiib*) The National Children Fund; or

(*iiic*) The Indira Gandhi Memorial Trust; or

(*iiid*) The Rajiv Gandhi Foundation; or

(*iiie*) The National Foundation for Communal Harmony; or

(*iiif*) A University or any educational institution of national eminence as may be approved by the prescribed authority;

(*iiig*) The Chief Minister's Earthquake Relief Fund Maharashtra

(*iiih*) The Zila Saksharta Samiti

(*iiiha*) The National Blood Transfusion Council or to any State Blood Transfusion Council which has its sole object of control, supervision, regulation or encouragement in India of the services related to operation and requirement of blood banks.

"National Blood Transfusion Council" means a society registered under the Societies Registration Act 1860 and whose Chairman is a person who is not below the rank of Secretary to the Government of India dealing with AIDS Control Project.

"State Blood Transfusion Council" means a society registered under the above mentioned Act and whose Chairman is Secretary to the State Government dealing with the Department of Health;

(*iiihb*) Any fund set up by a State Government to provide medical relief to the poor;

(*iiihc*) Army Central Welfare Fund, the Indian Naval Benevolent Fund or the Air Force Central Welfare Fund established by the armed forces of the union for the welfare of past and present members of such forces or their dependants;

(*iiihd*) The National Illness Assistance Fund;

(*iv*) Any other fund or any institution to which this section applies; or

With effect from assessment year 1998-99 100% deduction with no limit on amount donated shall be allowed on donation given to the Chief Minister's Relief Fund or the Lieutenant Governor's Relief Fund u/s 80G(1) (iiihf).

(*v*) The Government or any local authority, to be utilised for any charitable purpose other than the purpose of promoting family planning;

(*vi*) Any authority referred to in clause (20A) of a section 10, for the purpose of satisfying the need for housing accommodation or planning, development of cities, towns or villages or both; or

(*via*) Any corporation referred to u/s 10 (26 BB) *i.e.* a Corporation set up to promote the interests of minorities.

(*vii*) The Government or to any such local authority, institution or association as may be approved in this behalf by the Central Government to be utilised for the purpose of promoting family planning.

(*b*) Any sums paid by the assessee in the previous year as donation for the renovation or repair of any such temple, mosque, gurudwara, church or other place

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as notified by the Central Government in the Official Gazette to be of historic, archaeological or artistic importance or to be a place of public worship of renown throughout any State or States.

Under point (*v*) given above, any fund or institution to which this section (80G) applies needs careful understanding. It applies to donations to any institution or fund only if it is established in India for charitable purpose and it fulfils the following conditions:

(*a*) Where the institutions or fund derives any income and such income would not be liable to inclusion in its total income under the provisions of sections 11, 12 and sections 10(2), 10(22A), 10(22AA), 10(23AA) or 10(23C).

(*b*) Under its rules, no part of its income or assets is applicable to any non-charitable purpose.

(*c*) The institution or fund is not supposed to be for the benefit of any particular religion, community or caste.

(*d*) The institution or fund maintains regular accounts of its receipt and expenditure.

(*e*) It is either constituted as a public charitable trust or is registered under the Societies Registration Act, or under section 25 of Indian Companies Act, 1956, or is a university established by law, or is any other educational institution recognised by the Government or by a university or affiliated to any university established by law or is an institution financed wholly or in part by the Government or a local authority.

(*f*) Section 10(20A) includes an authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages.

(*g*) Donation given to Government or any approved local authority, institution or association for promoting family planning is also entitled for deduction under this section.

How to calculate amount qualifying for deduction u/s 80G

1. Calculate the qualifying amount for deduction:
   (*i*) *No limit donations:* Donations given to—
   (*a*) the National Defence Fund;
   (*b*) the Jawaharlal Nehru Memorial Fund;
   (*c*) the Prime Minister's Drought Relief Fund;
   (*d*) the Prime Minister's National Relief Fund;
   (*e*) the Prime Minister's Armenia Earthquake Relief Fund;
   (*f*) the National Children's Fund; and
   (*g*) the Indira Gandhi Memorial Trust (after 21.2.1985) shall fully qualify for deduction.
   (*h*) the Africa (Public contributions—India, Fund; with effect from 1.4.91) or
   (*i*) the Rajiv Gandhi Foundation (from assessment year 1992-93)

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(*j*) National Foundation for Communal Harmony [inserted by Finance Act, 1993]

(*k*) Any University or any educational institution of national eminence as may be approved by the prescribed authority;

(*l*) The Chief Minister's Earthquake Relief Fund Maharashtra;

(*m*) The Zila Saksharta Samiti.

(*n*) Any National Blood Transfusion Council or State Blood Tranfusion Council;

(*o*) Any fund set up by the State Government to provide medical relief to the poor;

(*p*) Army Central Welfare Fund; the Indian Naval Benevolent Fund or Air Force Central Welfare Fund;

(*q*) The National Illness Assistance Fund;

(*ii*) *With limit donations:* Donation given to—

(*a*) a State or Local Government;

(*b*) Some authorised body for promotion of family planning in India;

(*c*) any authority, prescribed by Government for this purpose; and

(*d*) any other fund constituted under the provisions of this section and which are given u/s 10 (23) and 10(23C) like Prime Minister's Student's Aid Fund or Folk Arts Fund.

shall qualify for deduction upto a limited amount. The limits are:

(*i*) Actual total donations given under this category; or

(*ii*) 10% of Gross Taxable Income; whichever is less.

Add the amount as aggregated in *no limit* category with the amount calculated under *with limit* category and this total is *qualifying amount (Q.A.).*

Gross Taxable Income means Gross Total Income minus all other tax-free incomes (*i.e.*, on which assessee is entitled to rebate of tax) and all other deductions except deduction u/s 80G.

Conditions:

No deduction to be allowed in case of the following donations:

1. Donations to political parties.
2. Donations in-kind.
3. Donations given are for the benefit of any particular religion, class, creed, community etc. However, donations given for the benefit of women and children, Scheduled Caste, Backward Classes or Scheduled Tribes etc. do not come in this category.
4. From 1.10.91, the benefit of section 80G can only be claimed if the Institution or Fund seeking donations has been approved by the commissioner of Income-tax.

   Provided that any approval shall have effect for such assessment year or years as may be specified in the approval but not exceeding three assessment years.

This deduction is allowed if the contribution is made out of taxable income of the assessee. If any contribution is made out of non-taxable income, no deduction will be allowed on that part of donation.

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In connection with donations "Charitable Purpose" does not include any purpose the whole or substantially the whole of which is of a religious nature.

Donation given to the sports association for promotion of sports and games in India also qualify for deduction under section 80G in the same manner as donations made to institutions or funds established in India for charitable purposes.

COMPUTATION AND RATES OF DEDUCTION U/S 80G—DONATIONS

Donation	*Q.A.*	*Rate*
A. No limit donations		
1. To P.M. National Relief Fund	100%	100%
2. To Africa Fund	100%	100%
3. To Armenia Earthquake Relief Fund	100%	100%
4. To University or institution of National Eminence (so notified)	100%	100%
5. To National Foundation for communal harmony	100%	100%
6. To the Chief Minister's Earthquake Relief Fund, Maharashtra	100%	100%
7. To Zila Saksharta Samiti	100%	100%
8. To National Blood Transfusion Council or State Blood Transfusion Council	100%	100%
9. To any fund set up by the State Govt. to provide medical relief to poor	100%	100%
10. To Army Central Welfare Fund, Indian Naval Benovelont Fund or Air Force Central Welfare Fund	100%	100%
11. To National Illness Assistance Fund	100%	100%
12. To National Defence Fund	100%	100%
13. To P.M. National Drought Relief Fund	100%	100%
14. To National Children's Fund	100%	100%
15. To Jawahar Lal Nehru Memorial Fund	100%	100%
16. To Indira Gandhi Momorial Trust	100%	100%
17. To Rajiv Gandhi Foundation	100%	100%
B. With limit donations		
1. To State Govt. 2. To Local Authority 3. To Educational Institutions 4. To Charitable Institutions 5. To Sports Institutions 6. To a corporation set up to protect the interests of minorities 7. To a place of art, public worship or historical importance (so notified) 8. To an institution or association engaged in promotion of family planning in India	Actual total of 1 to 8 or 10% of gross taxable income whichever is less is Q.A.	Out of Q.A. 100% of donation for F.P. and balance Q.A. 50%

G. Tax. I = G.T.I.—[Long term capital gain + All other deductions u/s 80 except 80GG + Rebateable income if any]

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Rebateable Income = Share of income from AOP or PFAOP provided total income of such AOP or PFAOP exceeds the exempted limit *i.e.* Rs. 40,000 and its income is not taxable at maximum marginal rate.

Rules :

1. Donation must not be given in kind.
2. Donation should not be given to a particular person.
3. Donation should not be given to a political party.
4. The institution or association to whom donation is given.
   - (*a*) must be a registered body,
   - (*b*) whose accounts are audited,
   - (*c*) which is notified for the time being under this section, and
   - (*d*) which is not meant for any particular caste, creed or religion.

Illustration 1. Mr. Soni whose gross total income is Rs. 40,00,000 makes the following donations during the previous year ending on 31.3.97 :

(*i*)	To Prime Minister's National Relief Fund	1,00,000
(*ii*)	To National Defence Fund	2,00,000
(*iii*)	To a temple of public worship for its repair (so notified)	2,00,000
(*iv*)	To a local college for construction of Commerce Block	1,00,000
(*v*)	To a poor student as aid	10,000
(*vi*)	To Municipal Committee	1,00,000
(*vii*)	To P.G.I. Chandigarh for promotion of Family Planning	50,000
(*viii*)	To Chief Minister's Earthquake Relief Fund Maharashtra	20,000

The gross total income includes Rs. 10,00,000 as his share from an associations of persons. Compute his total income for the assessment year 1997-98.

Solution. *Computation of deduction u/s 80G and total income*

Gross Total Income (including Rs. 10,00,000 as share from AOP)	40,00,000
Deduction u/s 80G (Note 1)	3,95,000
Total Income	36,05,000

Note 1

Sr. No.	*Donation*		*Q.A.*	*Rate*	*Amount*
No Limit Donations					
1.	To P.M. National Relief Fund		1,00,000	100%	1,00,000
2.	To National Defence Fund		2,00,000	50%	1,00,000
3.	To Chief Minister's Relief Fund Maharashtra		20,000	100%	20,000
With Limit Donations		Rs.			
1.	To a notified Temple	2,00,000	4,50,000	For F.P.	
2.	To a recognised College	1,00,000	or 10% of	50,000	
3.	To PGI for family planning	50,000	G. Tax I	100 % Balance	50,000
4.	To a Municipal Committee	1,00,000	3,00,000	Q.A.	
			w.e. less	2,50,000	
		4,50,000	is Q.A.	50%	1,25,000
	Deduction u/s 80G				3,95,000

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Q. No. 4

The gross total income of Mrs. Usha amounted to Rs. 6,00,000 in the previous year ending on 31st March, 1997. She has made the following donations :—

		Rs.
(*i*)	To Prime Minister's Armenia Earthquake Relief Fund	40,000
(*ii*)	To Africa (Public Contributions India) Fund	10,000
(*iii*)	To Approved Educational Institutions	15,000
(*iv*)	To Approved temples	35,000
(*v*)	Clothes distributed to poor	5,000
(*vi*)	To Municipal Corporation for promotion of family planning	20,000

Compute the amount of deduction admissible u/s 80G for the assessment year 1997-98. *[Karnataka B.Com. 1994]*

[**Hints :** Deduction u/s 80G Rs. 90,000]

Q. No. 5

Shri Anil earned gross total income of Rs. 5,00,000 in the previous year 1996-97 and made the following donations during the year :—

1. Rs. 10,000 to Chief Minister's Earthquake Relief Fund Maharashtra.
2. Rs. 15,000 to National foundation for Communal Harmony.
3. Rs. 40,000 to Municipal Corporation approved for promotion of family planning.
4. Rs. 25,000 to approved institutions.

Compute the amount of deduction admissible to him u/s 80G for the assessment year 1997-98. *[Karnataka B.Com. April, 1995]*

[**Hints :** Deduction u/s 80G Rs. 70,000]

8. Deduction in respect of Expenditure Incurred on Payment of House Rent (80GG)

Any assessee who is not receiving any income as specified in [section 10 (13A) *i.e.*, House Rent allowance] and is spending some part of his income as rent—on the furnished or unfurnished house, will be entitled to a deduction to the extent of least of the following:

(*i*) Excess of actual rent paid over 10% of his gross total income;

(*ii*) Rs. 2,000 p.m.; or

(*iii*) 25% of gross total income.

This deduction will not be allowed if a house is owned by assessee in his own name, or in the name of his spouse or minor child or if assessee is H.U.F. on the name of any member of family.

Gross total income means the income before allowing this deduction, *i.e.*, G.T.I. *less* [all deductions under section 80 and L.T.C. Gain].

To claim deduction u/s 80GG, the assessee must fulfil the following conditions:

1. The assessee (employee or self-employed) must be paying some rent in respect of any accommodation. The accommodation may be furnished or unfurnished.

2. The assessee must be paying rent over 10% of his gross total income (G.T.I. shall be as explained above).

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3. The assessee or his/her spouse or minor children of H.U.F. of which he is a member must not own any accommodation at a place where he ordinarily resides or his place of employment or profession is, and he should not own a self-occupied house property anywhere in India.

4. Under Income-tax Rules 11B, the assessee must have paid or incurred some expenditure towards payment of rent and the accommodation is situated in any of the 35 big cities, *i.e.*,

(*i*) Agra, Ahmedabad, Allahabad, Amritsar, Bangalore, Bhopal, Calcutta, Coimbatore, Delhi, Faridabad, Gawalior, Hyderabad, Indore, Jabalpur, Jaipur, Kanpur, Lucknow, Ludhiana City, Madurai, Nagpur, Patna, Poona, Srinagar, Surat, Baroda, or Varanasi, or the urban agglomeration of each of such places; or

(*ii*) Bombay, Calicut, Cochin, Ghaziabad, Hubli-Dharwar, Madras, Sholapur, Trivandrum or Vishakhapatnam.

(*iii*) The following explanation shall be inserted, namely:

Explanation—"Urban agglomeration", in relation to a place referred in this rule, means the area for the time being included in the urban agglomeration of such place for the purpose of grant of house rent allowance by the Central Government to its employees under the orders issued by it from time to time in this regard.

This deduction is being deleted with effect from assessment year 1998-99.

Illustration 2. If a professional man has his gross taxable income (*i.e.*, income before allowing this deduction) of Rs. 25,000 and pays rent of Rs. 600 p.m., calculate amount of deduction u/s 80GG.

Solution

He will be entitled to deduction as under, provided he fulfils all other conditions:

(*i*) Rent paid Rs. 7,200.
10% of Gross taxable income = Rs. 2,500
Excess = Rs. 4,700

(*ii*) 25% of G.T.I. = Rs. 6,250; or

(*iii*) Rs. 2,000 p.m., *i.e.*, Rs. 24,000.

He will be entitled to a deduction of Rs. 4,700 u/s 80GG.

Q. No. 6

Mr. Raman, a chartered accountant is living in Kanpur and is carrying on his profession there. For the year 1996-97 he has supplied the following information. Compute his total income for the assessment year 1997-98 :—

		Rs.
(*i*)	Professional Gain	62,400
(*ii*)	Rent received from a house at Delhi	18,000 p.a.
(*iii*)	Municipal Taxes for the house	1,500 p.a.
(*iv*)	Long Term Capital Gain	10,000
(*v*)	Part time salary as lecturer in taxation laws in local college	12,000 p.a.
(*vi*)	Rent paid for residential house	2,000 p.m.

[Hints : Deduction u/s 80GG Rs. 15,640 Total Income Rs. 71,960]

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9. Deduction in respect of any payment made to certain scientific institutions or an institution having rural development programme as its object [Section 80GGA]

The deduction shall be available to every such assessee, who during the previous year has made any payment:

(*a*) to a scientific research association which has as its object the undertaking of scientific research, or to a university, college or other institution, to be used for scientific research, and such bodies as are approved for the purpose of section 35(*i*), (*ii*);

(*aa*) any sum paid by the assessee in the previous year to a university, college or other institution to be used for research in Social Science or Statistical Research.

It is provided that such college, university or institution should be approved for purposes of section 35(1)(*iii*).

(*b*) (*i*) to an association or institution which has as its object the undertaking of any programme of rural development, to be used for carrying out any programme of rural development approved for the purposes of section 35CCA provided he furnishes the certificate as mentioned in section 35CCA from such association or institution (w.e. from 1984-85); or

(*ii*) to an institution or association which has as its object the training of persons for implementing programmes of rural development and such body is approved for the purposes of section 35CCA (2).

(*bb*) any sum paid by the assessee to a public sector company or a local authority or to an association or institution approved by the National Committee, for carrying out any eligible project or scheme referred to in section 35AC.

(*c*) any sum paid by the assessee in the previous year to an association or institution, which has as its object the undertaking of any programme of conservation of natural resources or of afforestation to be used for carrying out any programme of conservation of natural resources or of afforestation approved for the purposes of section 35CCB;

(*cc*) any sum paid by the assessee in the previous year to such fund for afforestation as is notified by the Central Govt. under section 35CCB (1b).

(*d*) any sum paid by the assessee in the previous year to a rural development fund to be set up and notified by the Central Government for the purposes of clause (*c*) of sub-section (1) of section 35CCA.

In this case any amount paid after 31.3.1983 will qualify for such deduction.

(*e*) National Poverty Eradication Fund (so notified).

The deduction will not be allowed in case of those assessees whose gross total income includes income which is chargeable to tax under the head "Profits and Gains of Business or Profession".

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DEDUCTIONS IN RESPECT OF CERTAIN INCOMES

The assessee earns certain incomes and a portion of such income is allowed as deduction.

1. Deduction in respect of new Industrial Undertaking or hotel set up in backward areas [Section 80HH]

Where an assessee has set up or sets up a new industrial undertaking or hotel in a backward area (as specified in 8th Schedule), he will be entitled to a deduction at the rate of 20% of profits and gains from such business for a period of 10 assessment years starting with effect from assessment year 1971-72. This deduction will be subject to following conditions:

Industrial Undertaking

(*i*) It has begun or begins to manufacture or produce articles after 31.12.1970 but before 1.4.1990 in any backward area;

(*ii*) It is not formed by the splitting up or the reconstruction of a business already in existence in any backward area (not applicable if business is re-established under the provisions of 33B);

(*iii*) It is not formed by the transfer to a business of machinery or plant previously used for any purpose in backward area;

(*iv*) It employs at least 10 workers or more in manufacturing process carried on with the aid of power or 20 workers or more working without the aid of power.

Hotel

(*i*) The business of hotel has started or starts functioning after 31.12.1970 but before 1.4.1990 in any backward area;

(*ii*) The business of the hotel is not formed by splitting up or the reconstruction of business already in existence;

(*iii*) The hotel is for the time being approved for the purpose by the Central Government.

Period of Deduction. The deduction is to be allowed for the period given below if the unit or hotel came into existence before 1.4.1973.

In case of industrial undertakings or hotels commencing work after 31.12.1970 but before 1.4.1973 tax deduction will be allowed from the assessment year 1974-75 and the term 10 assessment years shall refer to 10 assessment years as reduced by the number of assessment years which have expired before 1.4.1974, *e.g.*, if a hotel has started its work on 1st September 1971, it will be entitled to this deduction for 8 assessment years with effect from 1974-75.

Compulsory Audit. It will be necessary for non-corporate assessees to get their accounts audited if they want to claim this deduction.

Power of Assessing Officer. The Assessing Officer has been empowered to compute reasonable profits of such business if in his opinion it is difficult to compute profits of such business.

The Central Govt. has assumed the power to amend the 8th schedule as and when it feels necessary. As per notification dated 27.4.1983 the Govt. has classified

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the areas into A, B and C categories. Normally the districts included in A Group will be eligible for inclusion in 8th Schedule. Now as soon as Ministry of Industry declares an area as backward another notification will be issued to declare it backward. As such 8th Schedule has been omitted by Taxation Laws (Amendment) Act, 1986.

2. Deduction for Small Scale Industries [Section 80 HHA]

Where the gross total income of an assessee includes any profits and gains derived from a newly established small-scale undertaking, there shall be allowed a deduction of an amount equal to 20% of annual profit out of Gross Total Income. The small-scale industrial undertaking shall have to fulfil the following conditions to claim this deduction:

Conditions :

(*i*) It begins manufacture or produces articles after the 30th September 1977 but before 1.4.90 in any rural area.

(*ii*) It is not formed by the splitting up or the reconstruction of a business already set up; these condition shall not be applicable to the units re-established under the provisions of Section 33B.

(*iii*) It is not formed by the transfer to a new business of machinery or plant previously used for any purpose (20% of total value of plant and machinery can be previously used).

(*iv*) It is covered as factory under the provisions of Factories Act, *i.e.*, it employs, in the manufacturing process at least 10 workers in case power is used otherwise it should employ at least 10 workers.

Period. This deduction shall be allowed in respect of each of ten assessment years beginning with the assessment year relevant to the previous year in which the small-scale industrial undertaking begins to manufacture or produce articles. Since the amount of the deduction is to be calculated on the profits of the unit of that year, so if, in any of these years, there is no positive figure of profits, the allowance cannot be availed of in that year.

Audit. The assessee claiming this deduction must get his account audited from a Chartered Accountant and furnish certificate to this effect.

Other deductions. If the assessee is entitled to deduction u/s 80 I, the deduction u/s 80 HHA shall be allowed before allowing deduction u/s 80 I [as amended by Finance Bill (2) 1980].

Deduction under this section shall not be available to the small-scale units engaged in mining operations. The small-scale units eligible to deduction under section 80 HH or those who have already claimed deduction under section 80 HH, such units are not eligible to avail the deduction u/s 80 HHA. So the assessee can avail deduction either u/s 80 HH, or HHA.

Rural Area. It shall have the same meaning as assigned to it under the provision of section 35 CC.

Small-Scale Undertaking. It shall be an undertaking whose aggregate value of plant and machinery (other than tools, jigs, dies and moulds) on the last day of the previous year does not exceed Rs. 10 lakhs in case the previous year ends before 1st day of August 1980; Rs. 20 lakhs, in case where the previous year ends after 31st day of July 1980, but before 18 3.85 and Rs. 35 lakhs for previous year ending after 17.3.85.

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3. Deduction on account of Income from Foreign Contracts [Section 80 HHB]

Rate of deduction. In case a resident company or a person (other than a Co.) who is resident in India fulfils conditions given below, such assessee shall be entitled to a deduction of 50% of such profits and gains.

Conditions :

(*i*) Contracts should be with foreign Government or any statutory or other public authority, or agency in a foreign country or with a foreign enterprise.

(*ii*) The payment for the contract is received in foreign currency.

(*iii*) The contract is in respect of construction of building, road, dam, bridge or installation of any machinery or plant outside India.

(*iv*) 50% of profits has been transferred to a reserve which is shown in the Balance Sheet.

(*v*) 50% of profit in foreign exchange must be remitted to India within 6 months from the end of the relevant previous year.

In case reserve created or foreign exchange remitted to India is less than 50% of the profits, the deduction would be limited to that amount.

4. Deduction u/s 88HHC—Profit from Exports

(*i*) *Who can claim ?* This deduction is allowed to an Indian company or any other Resident non-corporate assessee.

(*ii*) *Eligibility.* Following types of persons who are engaged in export business can claim this deduction :—

A. Direct Exporters
   (*a*) of manufactured goods only;
   (*b*) of goods manufactured by others;
   (*c*) of manufactured goods as well as trading goods;

B. Supporting Manufacturer

C. Tea Business

(*iii*) *Export out of India.* This deduction can be claimed only if there are exports out of India. This term means that the goods must clear the custom barriers. Sale of goods taking place in a shop, emporium etc. shall not be called export.

Goods transferred to branch, warehouse, or any other establishment situated outside India and sale of such goods takes place from these institutions situated outside India, it shall also amount to export.

(*iv*) *Eligible Goods.* This deduction will be allowed only if there is export of goods and merchandise which is included in the 12th schedule. The goods shall not include services.

(*v*) *Repatriation of foreign Exchange.* The sale proceeds from the export of goods must be repatriated to India within six months from the close of previous year. This period can be extended only by the Chief Commissioner/Commissioner of Income-tax after recording the reasons. If sale proceeds are credited in a separate account approved by the Reserve Bank of India, such amount shall be deemed to have been repatriated

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provided it is credited within 6 months. In case trade is on government to government basis and the exporter gets payment of price in Indian currency, it shall also be eligible for this deduction.

(*vi*) *Compulsory Audit.* Any person who claims deduction under this section shall have to get his accounts audited as per provisions of this Act.

Computation of Deduction

1. Exporter of manufactured goods

Amount of deduction u/s 80HHC =

[N.P.×E.T/T.T.] + [90% of E.I.×E.T./T.T.]

N.P. (Net Profit). Income under the head "Profits and Gains" less

(*i*) 90% of Export Incentives,

(*ii*) 90% of receipts by way of brokerage, commission, interest and rent,

(*iii*) profits of any branch, warehouse, or other similar establishment situated outside India.

E.T. (Export Turnover). Sale Price of the goods exported in convertible foreign exchange less freight and insurance charges on such exports.

T.T. (Total Turnover). Total turnover of the year less (freight and insurance charges on such goods + export incentives)

E.I. (Export incentives). Profit on sale of export license + Export subsidy received + Duty drawback.

Illustration. 3. From the figures given below calculate amount of deduction admissible u/s 80HHC :--

	Rs.
(*i*) Total turnover during the year	60,00,000
(*ii*) Net Profit including export subsidy of Rs. 4,00,000	12,00,000
(*iii*) Export turnover (Out of which foreign exchange worth only Rs. 24,00,000 was remitted to India during the prescribed period)	30,00,000
(*iv*) Freight and insurance charges for the exports are	2,00,000.

Solution : *Computation of deduction u/s 80HHC*

	Rs.
(*i*) Net profit	12,00,000
Less: 90% of Export Incentive [90% of Rs. 4,00,000]	3,60,000
N.P.	8,40,000
(*ii*) Export Turnover (amount of foreign exchange remitted to India within prescribed time)	24,00,000
Less: Freight and insurance charges	2,00,000
E.T.	22,00,000

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(*iii*) Total Turnover	60,00,000
Less: Freight and insurance charges	2,00,000
T.T.	58,00,000

Ded. u/s 80HHC = 8,40,000 × 22,00,000/58,00,000 + 3,60,000 (90% of E.I.) × 22,00,000/58,00,000 = Rs. 3,18,621 + 1,36,552 = 4,55,173.

Q. No. 7

Compute amount of deduction u/s 80HHC admissible to M/s Zee Ltd. for the assessment year 1997-98 from the particulars given below :

Particulars	Rs.	*Particulars*	Rs.
To Business Expenses	82,00,000	By Export Sales	92,00,000
To Freight & Insurance (from Bombay port to Tokyo)	2,00,000	By Export Subsidy	14,00,000
To Net Profit	23,10,000	By Rent	50,000
		By Profit from branch at Singapur	60,000
Total	107,10,000	Total	107,10,000

Note : Out of export sales of Rs. 92,00,000 only Rs. 77,00,000 have been received in convertible foreign exchange in India upto 30th September 1997.

[**Hints :** Deduction u/s 80HHC = [9,45,000 × 75,00,000/90,00,000) + (12,60,000 × 75,00,000/90,00,000) = Rs. 7,87,500 + 10,50,000 = 18,37,500)]

2. Export of goods manufactured by others

Amount of deduction u/s 80HHC = [E.T. Less D.C. Less I.D.C.] + [90% of Export Incentives) × E.T./T.T.]

E.T. (Export Turnover) = Same as in 1 above.

T.T. (Total Turnover) = Same as in 1 above.

E.I. (Export Incentives) = Same as above in 1 above.

D.C. (Direct cost) = Purchase price of goods + cost directly attributable to such goods.

I.D.C. (Indirect cost) = (Total cost less Direct Cost) × E.T./T.T.

3. If disclaimer certificate is issued by export house/trading house in favour of a supporting manufacturer

The deduction for export house/trading house u/s 80HHC shall be reduced by an amount equal to Export Profit × value of disclaimer certificate/Export Turnover of Trading house.

4. Export of manufactured as well as trading goods

Deduction u/s 80HHC shall be calculated in following manner :—

A. Profit on trading goods =

E.T. of trading goods – (D.C. of trading goods +

I.D.C. of trading goods)

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B. Profit of manufactured goods =

Adjusted N.P. × adjusted E.T./Adjusted T.T. N.P. = Profit as per profits and gains [90% of Export Incentives + 90% of Rent, Brokerage, Commission, interest + Profits of foreign branch.]

Adjusted N.P. = N.P. – Profit on Trading goods;

Adjusted E.T. = E.T. – Turnover of Trading goods;

Adjusted T.T. = T.T. – Turnover of Trading goods.

C. Export Incentives. 90% of the amount of these incentives.

Total of amount arrived at "A", "B" and "C" is the amount of deduction to be allowed u/s 80HHC.

5. Deduction u/s 80HHC in case of Tea business

For the purposes of calculating this deduction Net Profit [N.P.] will be reduced to 40%.

Illustration. 4. Calculate the deduction admissible u/s 80HHC to a company, engaged in manufacture and sale of tea grown in own farms, from the following figures :—

Total sales of tea	Rs. 52,00,000
Export	Rs. 10,00,000
Total Profit	Rs. 10,00,000

Sale of Rs. 52 lakhs include Rs. 2 lakhs being the freight and insurance (beyond custom point) on export sales. *[Adapted C.A. Inter May, 1995]*

Solution : *Computation of deduction u/s 80HHC*

Net Profit (N.P.) (40% of Rs. 10,00,000)		Rs. 4,00,000
Total Turnover (T.T.)	Rs. 52,00,000	
Less: Freight and Insurance	Rs. 2,00,000	
T.T.	Rs. 50,00,000	
Export Turnover (E.T.)		Rs. 10,00,000

Deduction u/s 80HHC = Rs. 4,00,000 × Rs. 10,00,000/Rs. 50,00,000 = Rs. 80,000.

Deduction u/s 80 HHC for supporting manufacturers [80 HHC(1A)]

In case a supporting manufacturer sells goods or merchandise to any Export House or Trading House and has obtained a certificate to this effect from such house, it shall be eligible to claim deduction @ 100% of profits derived by such person from sale of goods or merchandise to Export or Trading House.

The same terms and conditions are applicable for such supporting manufacturer as are applicable in case of a person who himself exports goods or merchandise from India.

With effect from assessment year 1993-94 only the profit from trading goods is to be reduced by the proportion of turnover of supporting manufacturer to total turnover of trading goods of assessee.

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6. Deduction in respect of earnings in convertible foreign exchange [Section 80 HHD]

Rate of deduction [80 HHD(1)]

Where an assessee, being an Indian Company or a person (other than Company) resident in India is engaged in the business of a hotel or of a tour operator, or of a travel agent, shall be allowed a deduction of a sum equal to the aggregate of—

(*a*) 50% of the profits derived by him from services provided to the tourists; and

(*b*) Out of the remaining profit, any part of profit which is debited to the P & L A/c and credited to the reserve account and to be utilized for the purposes of the business of the assessee.

Eligibility [80 (HHD)(2)]

This deduction is admissible only to services provided to foreign tourists, the receipts in relation to which are received by the assessee in convertible foreign exchange.

Any payment received by an assessee, who is engaged in the business of a hotel, or of a tour operator or of a travel agent, in Indian currency out of currency obtained by conversion of foriegn exchange brought into India through an authorised dealer, from [*another hotelier* (*with effect from assessment year 1995-96*], tour operator or a travel agent, shall be deemed to have been received by the assessee in convertible foreign exchange. The person making such payment must furnish a certificate in prescribed form indicating the amount received in foreign exchange and its conversion into Indian Currency.

Eligible Profits [80 HHD(3)]

(*a*) Where the business carried on by assessee consists exclusively of services provided to foreign tourists resulting in receipts in convertible foreign exchange the eligible profits shall be profits as computed under the head "Profit & Gain of Business or Profession."

(*b*) Where assessee is not carrying on exclusive business of services provided to foreign tourists the eligible profits shall be the proportionate profits which shall be calculated as under:

$$\text{Eligible Profits} = \text{Net Profit as per P \& L A/c} \times \frac{\text{Receipts in convertible foreign exchange}}{\text{Total Receipts}}$$

Utilisation of Reserve [80 HHD (4)]

The amount credited to reserve as per clause (b) of 80 HHD(1) as given earlier, shall be utilised by the assessee within a period of 5 succeeding previous years for the following purposes only:

(*i*) Construction of new approved hotels or expansions of existing approved hotels;

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(*ii*) Purchase of new cars and new coaches by travel agents;

(*iii*) Purchase of sports equipment for mountaineering, trekking, golf, river-rafting and other sports in or on water;

(*iv*) Construction of conference or convention centres;

(*v*) Any other facility to be notified by Central Government.

In case any amount so utilised leads to creation of any asset outside India, prior permission from prescribed authority must be obtained.

Non-Utilisation of Reserve [80 HHD(5)]

(*a*) In case any amount has been utilised for a purpose other than that as referred above, the amount so utilised shall be income of the year in which it is so misutilised.

(*b*) In case amount is not utilised within the prescribed period of 5 years, it shall be deemed as income of the previous year next following the previous year in which such period expires.

Production of Certificate [80 HHD (6)]

The income of the business must be got audited and a certificate in prescribed form must accompany the return of income of the previous year in which deduction is claimed.

7. Deduction in respect of Profits From Export of Computer Software etc. [Section 80 HHE]

(1) Where an assessee being an Indian Company or any other person (other than a company) resident in India, is engaged in the business of—

(*i*) export out of India of computer software or its transmission from India to a place outside India by any means;

(*ii*) providing technical services outside India in connection with the development or production of computer software;

100% of profits derived by the assessee from such business shall be allowed as deduction while computing the total income of the assessee.

(2) The above mentioned deduction shall be allowed only if the consideration in respect of the computer software is received in, or brought into, India by the assessee in convertible foreign exchange within a period of 6 months from the end of the relevant previous year & within such extended period as allowed by the Commissioner in this behalf.

8. Deduction in respect of Profits and Gains from industrial undertaking set up after certain date [Section 80 I]

Rate of Deduction

Where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking or a ship or the business of hotel, a deduction at the following rates shall be allowed:

(*i*) Non-corporate assessee—25% of profits and gains.

(*ii*) Company assessee—30% of profits and gains.

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Period of Deduction [80 I (5)]

(*a*) *Co-operative assessee.* This deduction shall be allowed in respect of initial assessment year, *i.e.*, the assessment year relevant to the previous year in which the industrial undertaking begins to manufacture, or produce articles or things, or to operate its cold storage plant or plants or ship is first brought into use or the business of hotel starts functioning and each of the *eleven* assessment years immediately succeeding such initial assessment year;

(*b*) *For all other assessees.* For initial assessment year (as defined above) and each of the *nine* assessment years succeeding the initial assessment year; and

(*c*) *For assessees carrying on the business of repairs of ocean-going ships.* For initial assessment year and each of the four assessment years succeeding the initial assessment year.

Eligibility

1. *Industrial Undertaking* [80 I(2)]. An industrial undertaking which fulfils and following conditions shall be eligible for this deduction:

(*a*) It is not formed by splitting up, or the reconstruction of a business already in existence;

(*b*) It is not formed by the transfer to a new business of machinery or plant previously used for any purpose;

(*c*) It is producing or manufacturing an article not included in 11th schedule. This provision shall not be applicable for a small-scale undertaking;

(*d*) It begins to produce or manufacture things or articles or to operate such plant at any time between 1.4.81 to 31.3.91;

(*e*) In case it is carrying on a manufacturing process, it employs ten or more workers; if power is used or employs twenty or more workers if power is not used.

(*f*) In case, a unit is re-established and claims rehabilitation allowance u/s 33B, condition given at (*a*) above shall not be applicable.

(*g*) In certain cases second-hand imported plant and machinery can be used provided it fulfils following conditions:

(*i*) plant or machinery was not at any time, prior to the date of its installation by the assessee, used in India;

(*ii*) such plant or machinery is imported into India from any country outside India; and

(*iii*) no deduction on account of depreciation in respect of such plant or machinery has been allowed or is allowed to any person prior to the date of installation of plant and machinery by assessee.

(*h*) In case, any plant or machinery is installed which had been previously used in India, the total value of such plant or machinery must not exceed 20% of the total value of machinery installed.

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2. *Ship* [80 I(3)]. This deduction can be claimed if any ship is acquired provided following conditions are fulfilled:

(*i*) It is owned by an Indian company and is wholly used for the purposes of business carried on by it;

(*ii*) It is not, prior to the date of its acquisition by Indian Company, owned or used in Indian territorial waters by a person resident in India; and

(*iii*) It is acquired at any time between 1.4.1981 to 31.3.1991.

3. *Hotel* [80 I(4)]. A Hotel which fulfils following conditions shall qualify for this deduction:

(*i*) It is not formed by splitting up or reconstruction of a business already in existence or by transfer of a building previously used as hotel to such new business.

(*ii*) The business of hotel is owned and carried on by a company registered in India with a paid-up capital of not less than Rs. 5 lakhs.

(*iii*) The business of the hotel starts functioning at any time between 1st April 1981 to 31st March, 1991.

(*iv*) The hotel is, for the time being, approved by the Central Government.

Other Conditions

1. While calculating the profit and gains of industrial undertaking, ship, hotel, or a cold storage plant, it shall be assumed that such industrial undertaking, ship, hotel, or cold storage were the only source of the income of assessee [80 I(6)].

2. For non-corporate assessees claiming deduction under this section audit by a chartered accountant shall be compulsory [80 I(7)].

3. In case some goods are transferred from the industrial undertaking or the hotel, or the operations of ship are transferred to any other business and *vice-versa*, and the consideration recorded for such transfer does not correspond with the fair market value, the profits and gains shall be computed taking into consideration the fair market value instead of original consideration [80 I(8)].

4. Where the I.T.O. finds that as a result of some close connections between the assessee and any other person, the profits of unit claiming deduction are shown at a higher level than what it is expected to earn, he may take the reasonable profits as may be deemed to have been derived from this business [80 I(9)].

9. Deduction in respect of profits and gains from Industrial Undertakings etc. in Certain cases [Section 80 (IA)]

The Finance Act (No. 2) 1991 has introduced this new deduction retrospectively from 1st April, 1991.

Where the gross total income of an assessee includes any profits and gains derived from any business of an Industrial undertaking or a Hotel or operation of a ship, *or developing, maintaining and operating any infra structural facility* or *scientific and industrial research and development* assessee shall be allowed a deduction while computing total income.

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Rates of Deduction u/s 80IA

Sr. No.	*Undertaking*	*Rate*		*Period*	
		Company	*Any other*	*Co-op.*	*Any other*
A.	**Industrial Undertaking**				
(*i*)	Engaged in generation or distribution of power	100%	100%	For first 5 years	5 years
		30%	25%	For next 7 years	5 years
(*ii*)	Set-up in notified backward areas (8th schedule)	Same as per above			
(*iii*)	In case of any other industrial undertaking	30%	25%	12 years	10 years
B.	**Hotels**				
(*i*)	Set-up in notified areas or rural area, or hilly area or place of pilgrimage	50%	Nil	Nil	10 years
(*ii*)	Set-up at any other place	30%	Nil	Nil	10 years
C.	**Ships**	30%	Nil	Nil	10 years
D.	**Any undertaking engaged in providing infrastructural facility**	100%	100%	For first 5 years	5 years
		30%	30%	Next 7 years	5 years
E.	**Carrying on scientific research and Industrial development**	100%	Nil	Nil	5 years for company only

ELIGIBILITY

1. *Industrial Undertaking* [80 IA(2)]. An industrial undertaking which fulfils the following conditions shall be eligible for this deduction:

(*a*) It is not formed by splitting up, or the reconstruction of a business already in existence;

(*b*) It is not formed by the transfer to a new business of machinery or plant previously used for any purpose;

(*c*) It is producing or manufacturing an article not included in 11th schedule. This provision shall not be applicable for a small-scale undertaking;

(*d*) It begins to produce or manufacture things or articles or to operate cold storage plant at any time between 1.4.91 to 31.3.95. This period can be extended by issuing a notification in official Gazette;

(*e*) (*i*) Industrial undertaking set up in notified backward areas (as notified in 8th schedule) and set up during 1.4.94 to 31.3.99.

(*ii*) Industrial undertaking set up during 1.4.93 to 31.3.98 and engaged in generation or distribution of power.

(*iii*) Industrial undertaking set up during 1.4.91 to 31.3.2000 provided it is in small scale sector.

(*iv*) Any other industrial undertaking which had been set up during 1.4.91 to 31.3.95.

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(*f*) In case, it is carrying on a manufacturing process, it employs ten or more workers if power is used or employs twenty or more workers if power is not used.

(*g*) In case, a unit is re-established and claims rehabilitation allowance u/s 33B, condition given at (*a*) above shall not be applicable.

(*h*) In certain cases second-hand imported plant and machinery can be used provided it fulfils following conditions:

(*i*) plant or machinery was not at any time, prior to the date of its installation by the assessee, used in India;

(*ii*) such plant or machinery is imported into India from any country outside India; and

(*iii*) no deduction on account of depreciation in respect of such plant or machinery has been allowed or is allowed to any person prior to the date of installation of plant and machinery by assessee.

(*i*) In case, any plant or machinery is installed which had been previously used in India, the total value of such plant or machinery must not exceed 20% of the total value of machinery installed.

2. *Ship* [80 IA(3)]. This deduction can be claimed if any ship is acquired provided following conditions are fulfilled:

(*i*) It is owned by an Indian company and is wholly used for the purposes of business carried on by it;

(*ii*) It is not, prior to the date of its acquisition by Indian Company, owned or used in Indian territorial waters by a person resident in India; and

(*iii*) It is brought into use by the Indian company during 1.4.91 to 31.3.95.

3. *Hotel* [80 IA(4)]. A Hotel which fulfils the following conditions shall qualify for this deduction:

(*i*) It is not formed by splitting up or reconstruction of a business already in existence or by transfer of a building previously used as hotel to such new business;

(*ii*) The business of hotel is owned by and carried on by a company registered in India with a paid up capital of not less than Rs. 5 lakh;

(*iii*) The business of the Hotel located in a hilly area or a rural area or a place of pilgrimage or such other place as the Central Government may having regard to the need for development of infrastructure for tourism in any place and other relevant considerations specify for the purpose of this clause, starts functioning at any time during the period beginning on the 1st day of April 1990 and ending on 31.3.1994; or

(*iv*) The business of the hotel—(*a*) located in any place; or (*b*) located in a place other than referred to in clause (*iii*) above starts functioning during 1.4.91 to 31.3.95.

4. *Enterprises engaged in developing maintaining and operating any infrastructure facility (Section 80 IA (4A)]*

(*i*) The enterprise is owned by a company registered in India or by a consortium of such companies.

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(*ii*) The enterprise has entered into agreement with Central or State Government, Local authority or any other statutory body for developing, maintaining or operating new infrastructure facility to be transferred to the Central or State Government, Local authority or such other statutory body after stipulated period.

(*iii*) The enterprise starts operating after 1-4-95.

5. Companies engaged in scientific and industrial research and Development [Section 80IA (4B)]

This section shall be applicable to an Indian company which is carrying on scientific and industrial research and development and which fulfills the following conditions :

(*i*) The company has the main object of scientific and industrial research and development and

(*ii*) The company is for the time being approved by the prescribed authority at any time before 1.4.1998.

Period of Deduction [Section 80 IA(6)]

(*i*) *Co-operative Society assessee.* Deduction shall be allowed for initial year & *eleven* subsequent years, thus allowing this deduction for 12 years.

(*ii*) *Any other assessee.* Deduction shall be allowed for 10 years *i.e.* initial year & *nine* subsequent years in case of any other assessee deriving profits and gains from an Industrial undertaking.

(*iii*) *Assessees deriving profits & gain from a ship or a Hotel.* Deduction allowed only for 10 years *i.e.* initial year and nine subsequent years.

(*iv*) For enterprises engaged in developing maintaining and operating infrastructure facilities—deduction will be allowed for 10 successive assessment years.

(*v*) For companies engaged in scientific research and industrial development deduction will be allowed for a period of 5 years from the assessment year relevent to the previous year in which the company is approved by the prescribed authority for this purpose.

Deduction to be allowed only out of the profits of eligible unit [80 IA(7)]

Deduction under this section is to be allowed only if such eligible business is only source of income in the initial assessment year and subsequent assessment years for which deduction is admissible.

Compulsory Audit [80 IA(8)]. In case deduction under this section is claimed by a person other than company or a co-operative society, a report of audit by a Chartered Accountant must accompany the return relating to the previous year in which such deduction is claimed.

Adjustment of Profits [Section 80 IA (a) and (10)]. In case there is transfer of any goods held for the purposes of eligible business to any other business and price does not correspond to fair market value, the profits of eligible business shall be adjusted taking fair market value as the price.

Further, in case Assessing Officer is of the opinion that the profits of the eligible business are unnecessarily inflated, he may make the necessary adjustments.

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Powers of the Central Govt. [80 IA (11)]

Central Govt. may by notification in Official Gazette withdraw this deduction and may specify the date of such withdrawal.

Definition of certain terms [80 IA (12)]

(*i*) *Hilly area* means any area located at a height of one thousand metres or more above sea level.

(*ii*) *Initial assessment year* means the assessment year relevant to the previous year in which industrial undertaking begins to manufacture or produce articles or things or to operate its cold storage plant or plants or the ship is first brought into use or the business of hotel starts functioning.

(*iii*) Small scale industrial undertaking with effect from assessment year 1993-94 the small scale unit means a small scale industrial undertaking which is regarded as such on last day of the previous year under section 11B of the Industries (Development and Regulation) Act 1951.

(*iv*) *"Infrastructure facility"* means

(*a*) a road, highway, airport, port, rail system, or any other public facility of similar nature as may be so notified,

(*b*) a water supply project, irrigation project, sanitation of sewerage system.

10. Deduction in respect of profits and gains from business of poultry farming [Section 80 JJ]

With effect from assessment year 1990-91 a deduction @ $33^1/_3$% of profits and gains derived from business of poultry farming shall be allowed to an assessee if its gross total income includes such profits.

11. Deduction in respect of interest on certain securities, dividends, etc. or deduction in respect of other investment incomes [Section 80L]

This section is very important to a large number of assessees as through this section, the assessees have been encouraged to invest their funds in certain specified fields and income from such investments is allowed as deduction up to some fixed amount. An assessee is allowed a deduction of Rs. 12,000 or actual income from such investments, whichever is less. This deduction is permissible in case the income is from the following investments:

(*a*) Interest on Government securities (Central or State Government, including interest on National Savings Certificates) (*vi*), (*vii*) or (*viii*) issue.

(*b*) Dividends from any Indian Company.

(*c*) Dividends received from any Co-operative Society.

(*d*) Incomes received from the Unit Trust of India in respect of units.

(*e*) Interest on deposits under-national deposit scheme.

(*f*) Interest on deposits made under any scheme framed by the Central Government and notified by it on this behalf, *e.g.*, interest on compulsory Deposit (Salaries) and (Tax-payers) Schemes.

(*g*) Interest on deposits with banking company (including Co-operative Banks) and other Banks (including IDBI).

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(*h*) Interest on deposits with a financial corporation engaged in providing long-term industrial finance in India and approved by the Central Government.

(*i*) Interest on deposits with a co-operative society of which the assessee is a member.

(*j*) Interest on deposits with any authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and village or both.

(*k*) Interest on deposits with a financial corporation which is engaged in providing long-term finance for industrial development in India or with a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes.

(*l*) Interest on debentures issued by an institution or authority, or by any public sector company or any co-operative society (including a co-operative land mortgage bank or co-operative land development bank) so notified by the Central Government.

(*m*) Income received in respect of Units of a Mutual Fund specified under section 10(23D).

(*n*) Interest on deposits under Post Office (Monthly Income Account) Rule 1987.

The deduction under Section 80L is allowed only to the following assessee:

(*i*) an individual, or

(*ii*) a Hindu undivided family, or

Rate of deduction

(*i*) A deduction of actual total or Rs. 12,000 p.a. whichever is less shall be allowed.

(*ii*) In case the total of eligible incomes includes—

(*a*) Dividend from an Indian Company,

(*b*) Income in respect of units of UTI, or

(*c*) Income in respect of units of Mutual Fund specified under section 10(23D)

An additional deduction of Rs. 3,000 or excess of these incomes over Rs. 12,000 whichever is less shall be allowed.

Illustration 5. From the particulars given below calculate the amount of deduction u/s 80L:

(A)		Rs.
(*i*)	Interest on Bank deposits	10,000
(*ii*)	Dividend from Indian Company	4,000
(*iii*)	Interest on Units of UTI	1,000
(*iv*)	Income on Mutual Fund set up under section 10(23D)	1,500

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		Rs.
(B)		
(*i*)	Dividend from Indian companies	2,000
(*ii*)	Dividend from a Foreign company	3,000
(*iii*)	Interest on Govt. Securities	800
(*iv*)	Interest on debenture of a Public Ltd. Co.	4,000
(*v*)	Interest on NSC (VIII issue)	2,000
(C)		
(*i*)	Interest on NSC VIII issue	6,000
(*ii*)	Interest on Govt. securities	7,000
(*iii*)	Dividend from a foreign company	4,000
(*iv*)	Dividend from an Indian Co.	1,000
(*v*)	Interest on units of U.T.I.	1,500

Solution

Calculation of deduction u/s 80L

(A) Total amount eligible for 80L

	Rs.
Interest on Bank deposits	10,000
Dividend from companies	4,000
Interest on units of UTI	1,000
Interest on units of Mutual Fund	1,500
Total	16,500

Deduction u/s 80L : Actual Total Rs. 16,500 or
(Rs. 12,000 + 3,000) w.e. is less. So Rs. 15,000 shall be allowed as deduction.

(B) *Eligible Income for deduction u/s 80L*

	Rs.
Dividend from Indian company	2,000
Interest on Govt. securities	800
Interest on N.S.C. (VIII issue)	2,000
Total	4,800

Deduction u/s 80L : Actual Total Rs. 4,800 or
(Rs. 12,000 + 3,000) w.e. is less. So Rs. 4,800 shall be allowed as deduction.

(C) *Qualifying Amount for deduction u/s 80L = Rs. 15,500*

Deduction u/s 80L Rs. 14,500. First step. Rs. 12,000 for interest on NSC VIII issue + Interest on Govt. securities and Rs. 2,500 extra for dividend from Indian Co. and Interest on units of U.T.I. Total deduction = Rs. 14,500.

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Q. No. 8

From the particulars given below calculate the amount of deduction admissible to :

(*a*) an individual,

(*b*) a firm assessed as firm,

(*c*) a company

Incomes	Rs.
(*i*) Interest on bank deposits	2,400
(*ii*) Interest on N.S.C. VIII issue	3,000
(*iii*) Interest on Govt. Securities	1,800
(*iv*) Interest on listed debentures of a Co.	4,000
(*v*) Dividend from Indian company	2,500
(*vi*) Interest on co-op. debentures	3,000
(*vii*) Dividend from a foreign company	6,000

[**Hints :** (*a*) Incomes at (*i*), (*ii*), (*iii*), (*v*) and (*vi*) to qualify. Deduction u/s 80L Rs. 12,000 + Additional deduction Rs. 700 = Rs. 12,700.

(*b*) and (*c*) PFAF and Company cannot claim this deduction.]

12. Deduction in respect of royalties, etc., received from certain foreign companies [80-O]

A deduction under this section is allowed for an amount equal to 50% of such amount with effect from assessment year 1985-86 where any income by way of royalty, commission, fees, etc., from a foreign concern is received by an Indian company or a person (other than company) who is resident in India. This section grants deduction of the whole of such income received from a foreign company in consideration for the use of any patent, invention, mode, design, secret formula or process or similar property right or information concerning industrial, commercial or scientific knowledge, experience or skill made available to the foreign Government or foreign enterprises. The receipt of such income may be in consideration of technical or professional services rendered outside India to such foreign Government or enterprises by the assessee.

From the assessment year 1975-76 this deduction stands discontinued in the case of resident non-corporate assessee and a provision has been made, by retrospective amendment, to provide that the deduction under this section will be allowed only to the extent that such income is received in accordance with foreign exchange law.

13. Deduction in respect of income of Co-operative Societies [Section 80 P]

Section 80 P provides for certain deductions to be made in computing the total income of a co-operative society. They are as under:

(*a*) In the case of a co-operative society engaged in—

- (*i*) carrying on the business of banking or providing credit facilities to members, or
- (*ii*) a cottage industry, or
- (*iii*) the marketing of the agricultural produce of its members, or
- (*iv*) the purchase of agricultural implements, seeds, livestock or other articles intended for agriculture for the purpose of supplying them to its members, or
- (*v*) the processing, without the aid of power, of the agricultural produce of its members, or

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(*vi*) the collective disposal of the labour of its members, or

(*vii*) fishing or allied activities.

(*b*) In the case of a primary co-operative society engaged in supplying *milk, oil seeds, fruits or vegetables* raised by its members to

(*i*) a federal co-operative society *engaged in the business of supplying milk, oil seeds, fruits or vegetables;*

(*ii*) the Government or a local authority; or

(*iii*) a Government company as defined in section 617 of the Companies Act, 1956 or a Corporation set up by Central or State Government (being a company engaged in supplying milk to the public).

The whole of amount of profits and gains of such business [*i.e.,* (*a*) and (*b*) above] shall be deducted from the gross total income.

(*c*) In the case of a co-operative society engaged in activities other than those specified in clause (*a*) or clause (*b*) profits and gains attributable to such activities *to the extent of* Rs. 40,000 *shall be deducted* from the gross total income.

(*d*) In the case of every co-operative society *the whole of the income; by way of interest or dividends* derived from its investment with any other co-operative society, shall be deducted from the gross total income.

(*e*) In the case of every co-operative society the *whole of the income,* derived by the society from the letting of godowns or warehouses for storage, processing or facilitating the marketing of commodities, shall be deducted from the gross total income.

(*f*) In the case of a co-operative society, not being a housing society or an urban consumers society or a society carrying on transport business or a society engaged in the performance of any manufacturing operations with the aid of power, where the gross total income does not exceed Rs. 20,000 *the amount of any interest from securities or any income from property* shall be deducted from the gross total income.

If the society is also entitled to the deduction under section 80 HH, the deduction in relation to the sum specified in the aforesaid clauses (*a*), (*b*) or (*c*) shall be allowed after allowing the deduction under section 90 HH.

14. Deduction in Respect of Profits and Gains from the Business of Publication of Books [Section 80-Q]

Where in case of an assessee the gross total income includes any profits and gains derived from a business carried on in India of printing and publications of books or publication of books, a deduction @ 20% of such profits shall be allowed. Deduction under this section shall be allowed for the assessment year 1992-93 and four assessment years next following that assessment year. **As such it stands withdrawn from assessment year 1997-98.**

Keeping in view the vital role played by the publishing industry in the development of human resources, the deduction u/s 80Q shall be allowed for a period of five years commencing from assessment year 1992-93. (Circular No. 706 dated 26.6.95).

The amount of total income shall be reduced by the amount of deduction, if any, admissible to the assessee under Section 80 HH, 80 HHA, 80 HHC, 80-I, 80-1A, 80 J or 80 P of this act.

For the purposes of this section, the word 'books' shall not include newspapers, journals, magazines, diaries, brochures, tracts, pamphlets and other publications of a similar nature by whatever name called.

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15. Professional Income of Authors of Text Books in Indian Languages [Section 80 QQA]

The Finance Act (No. 2) 1991 has re-introduced this deduction from the assessment year 1992-93 for a period of 5 years.

If any assessee earns any income as author of text books in Indian languages and such income has been included in the gross total income of the assessee, 25% of income from such books shall be allowed as deduction while calculating total income of the assessee.

The book should be a standard text book prescribed for a degree or post-graduate course of a university in any language specified in the Eighth Schedule of the constitution or in any other language as the Central Govt. may notify. **This deduction stands withdrawn from assessment year 1997-98.**

16. Remuneration earned outside India by professors, teachers, etc. [Section 80 R]

This deduction is allowed to such individuals and citizens of India, who earn some income in their capacity as professor, teacher or research workers in a University, College and educational institutions established outside India. The remuneration received should be from outside India and from the work done in the educational institutions.

A deduction equal to 75% of such remuneration as is brought into India by or on behalf of the assessee in convertible foreign exchange within a period of six months from the end of the previous year or within such extended period as the Chief Commissioner or the Commissioner may allow. Assessee must furnish a certificate that the deduction has been correctly claimed.

17. Deduction in respect of professional income from foreign sources in certain cases [Section 80 RR]

Deduction under this section is allowed to certain categories of professional individuals, who are residents of India and earned any income from outside India through their professional intelligence, skill as an author, playwright, artist, musician or actor. The income should be from a foreign Government or any other person not resident in India. Again, this deduction is allowed if he fulfils all the requirements of Foreign Exchange Regulation Act, 1974.

A deduction equal to 75% of such remuneration as is brought into India by or on behalf of the assessee in convertible foreign exchange within a period of six months from the end of the previous year or within such extended period as the Chief Commissioner or the Commissioner may allow. Assessee must furnish a certificate that the deduction has been correctly claimed.

Photographers, television cameramen are regarded as 'artists' for the purpose of this section. The Finance Act (2) 1980 has extended this benefit to sportsmen also.

18. Deduction in respect of remuneration from foreign employers [Section 80 RRA]

When the gross total income of an individual, who is a citizen of India, includes any remuneration received by him from any employer (being a foreign employer of an Indian concern) for any service rendered by him outside India, such individual shall be allowed.

A deduction equal to 75% of such remuneration as is brought into India by or on behalf of the assessee in convertible foreign exchange within a period of six

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months from the end of the previous year or within such extended period as the Chief Commissioner or the Commissioner may allow. Assessee must furnish a certificate that the deduction has been correctly claimed.

The individual must, if already in service of Central or State Government, be sponsored by his employer Government and if he is any other employee he must be technician whose contract of service is approved by the Central Government.

19. Deduction in case of blind or physically handicapped resident persons [Section 80U]

An individual resident of India and who is totally or partially blind or mentally retarded or permanently physically handicapped which reduces his earning capacity substantially is allowed a deduction of Rs. 40,000 *[Rs. 20,000 upto assessment year 1995-96]* from his gross total income if he suffers from this disability in the previous year.

The assessee must fulfil the following two conditions in the first assessment year in which he claims deduction under this section:

(*i*) if he is blind, certificate as to his total or partial blindness from a Registered Medical Practitioner (R.M.P.), being an eye specialist; or

(*ii*) a medical certificate from R.M.P. showing his permanent physical disability; or

(*iii*) certificate as to the mental retardation from a psychiatrist working in Government hospital.

The Central Board of Direct Taxes has declared in its Notification No. 142/24/90TOL NO 8986 Dt. 27.1.92 that Section 80U, of the I.T. Act, 1961 providing a deduction of Rs. 40,000 in cases if a person suffers from the following permanent physical disabilities;

(*i*) Permanent physical disability shall be regarded as a permanent physical disability if it falls in any one of the categories specified below, namely:

- (*a*) permanent physical disability of more than 50 per cent in one limb; or
- (*b*) permanent physical disability of more than 60 per cent in two or more limbs; or
- (*c*) permanent deafness with hearing impairment of 71 decibels and above; or
- (*d*) permanent and total loss of voice;

(*ii*) mental retardation shall be regarded as a mental retardation if intelligence quotient is less than 50 on a test with a mean of 100 and a standard deviation of 15 such as the Wechsle scale."

(*iii*) blindness shall be regarded as a permanent physical disability, if it is incurable and falls in any one of the categories specified below namely:

	All with corrections	
	Better eye	Worse eye
(*a*)	6/60 to 4/60 or Field of vision 110-20	3/60 to Nil
(*b*)	3/60 to 1/60 or Field of vision 100	F.C. at 1 foot to Nil
(*c*)	F.C at 1 foot to Nil or Field of vision 100	F.C. at 1 foot to Nil or Field of vision 100
(*d*)	Total absence of sight	Total absence of sight.

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CHART SHOWING COMPUTATION OF DEDUCTIONS UNDER SECTION 80 OUT OF GROSS TOTAL INCOME

Section	*Deduction*	*Who can Claim*	*Qualifying Amount*	*Period*	*Rate*
1. 80 CCC	Pension Fund	Individual	Any amount paid to LIC under pension fund set up u/s 10 (23AB)	Every year	Actual amount paid or Rs. 10,000 p.a. which ever is less
2. 80 D	Health Insurance	Individual & HUF	Amount paid to G.I.C. for health insurance (Mediclaim)	Every year	Actual Amount paid or Rs. 6,000 whichever is less
3. 80 DD	Medically Handicapped dependent	-do-	Any amount spent on training treatment or rehabilitation	-do-	Rs. 15,000 p.a.
4. 80 DDA	Deposit with LIC or UTI	Individual & HUF only (Resident)	For making a deposit with L.I.C. or U.T.I under a scheme to provide annuity to a mentally retarded or physically handicapped dependent	Every year	Rs. 20,000 p.a.
5. 80 DDB	Expenses on treatment	Individual & HUF	Expenditure incurred on treatment of self, dependent member of family or on any member of HUF who is suffering from a notified disease	Every year	Rs. 1,500 p.a.
6. 80 E	Repayment of Loan taken for higher education	Individual only	Amount repaid against loan taken for his higher education. Loan must be taken from any financial institution or approved institution	Every year	Actual Amount repaid or Rs. 25,000 w.e. is less
7. 80 G	Donations to approved funds and institutions	All assessees	*Donation*	*Q.A.*	*Rate*
			A. No limit donations		
			1. To P.M. National Relief Fund	100%	100%
			2. To Africa Fund	100%	100%
			3. To Armenia Earthquake Relief Fund	100%	100%
			4. To University or institution of National Eminence (so notified)	100%	100%
			5. To National Foundation for communal harmony	100%	100%
			6. To the Chief Minister's Earthquake Relief Fund, Maharashtra	100%	100%
			7. To Zila Saksharta Samiti	100%	100%
			8. To National Blood Transfusion Council or State Blood Transfusion Council	100%	100%

Section	Deduction	Who can Claim	Qualifying Amount	Period	Rate
			9. To any fund set up by the State Govt. to provide medical relief to poor	100%	100%
			10. To Army Central welfare Fund, Indian Naval Benovelont Fund or Air Force Central Welfare Fund	100%	100%
			11. To National Illness Assistance Fund	100%	100%
			12. To National Defence Fund	100%	50%
			13. To P.M. National Drought Relief Fund	100%	50%
			14. To National Children's Fund	100%	50%
			15. To Jawahar Lal Nehru Memorial Fund	100%	50%
			16. To Indira Gandhi Momorial Trust	100%	50%
			17. To Rajiv Gandhi Foundation	100%	50%
	is not taxable at MMR		**B. With limit donations**		
			1. To State Govt.	Actual total of 1 to 8 or 10% of gross tax-able income whichever is less is Q.A.	Out of Q.A. 100% of donation for F.P. and balance Q.A. 50%
			2. To Local Authority		
			3. To Educational Institutions		
			4. To Charitable Institutions		
			5. To Sports Institutions		
			6. To a corporation set up to protect the interests of minorities		
			7. To a place of art, public worship or histo-rical importance (so notified)		
			8. To an institution or association engaged in promotion of family planning in India		
			G. Tax. I = G.T.I.—(long term capital gain + All other deductions u/s 80 except 80GG + Rebateable income, if any) **Rebateable Income** = Share of income from AOP or PFAOP provided total income of such AOP or PFAOP exceeds the exempted limit *i.e.* Rs. 40,000 and its income is not taxable at MMR.		
8. 80 GG	**Payment of House Rent in certain cases only**	*Individual*	(*a*) He is living in a rental house at a place included in the list of towns given in Income-tax Rules 11B; (*b*) He and any of his family members or HUF (whose member he is) does	Every year in which house rent is paid.	(*i*) Rs. 2,000 p.m., (*ii*) 25% of Gross Total Income; (*iii*) Excess of rent paid over 10%

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			not own any residential house at the place where he is living; and (*c*) If he is having a residential house at some other place then the same is not being claimed as a self-occupied house. (*d*) He is not getting any H.R. Allowance from any source.		of G.T.I. whichever is less is allowed as a deduction. (G.T.I. for this purpose means the gross total income minus all other deductions and LTCG)
9. 80 GGA	**Donation given for rural development programme or scientific research**	All such assesses except those who have any income or loss under the head Profits & Gains of Business or Profession.	(*i*) Donation given to institution, or association engaged in scientific research and approved for the purpose. (*ii*) Donation given to institution or association engaged in approved rural development programme or conservation of natural resources or afforestation. (*iii*) Donation given to institution engaged in training of persons for rural development programme. (*iv*) any amount given to a Rural Development Fund (from 1.4.83 onwards). (*v*) any amount given to fund for afforestation (*vi*) any amount given by assessee to a University, College or other institution (so notified) for research in social science or statistical research. (*vii*) any amount paid by assessee to a public sector company or a local authority or to an institution or association approved by the National Committee for carrying out any eligible project or scheme. (*viii*) Fund set up for eradication of poverty.	Every year in which such amount is given.	Actual expenditure is fully allowed.
10. 80 HHB	**Deduction of income from foreign contracts**	All resident Indians and Indian companies	Profits from: (*a*) Contracts with foreign governments or statutory or other public authority of a foreign Government. (*b*) received in foreign currency.	Every year in which such profits are received.	50% of profits of such contract.

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Section	Deduction	Who can Claim	Qualifying Amount	Period	Rate
			(*c*) a reserve of 50% of profits from such contract has been created in balance sheet. (*d*) 50% of the profits have been remitted to India in foreign exchange within 6 months.		
11. 80 HHC	**Deduction from Profits earned from exports**	-do-	When there are profits from exports carried on by assessee during relevant previous year.	Every year with effect from 1984-85	100% of profit
12. 80 HHD	**Deduction for earnings in convertible foreign exchange**	All resident assessees and Indian company	Profit of— services provided to tourists if earned in convertible foreign exchange	Every year	50% of such profits + any amount transferred to a reserve.
13. 80 HHE	**Deduction for profits from export of computer software**	All resident assessees and Indian companies	Profit from export of computer software or its Transmission outside India	Every year	100% of profits from such business
14. 80 I	**Deduction for setting new industrial undertaking**	All assessees	Profits of— (*i*) an industrial undertaking which starts functioning after 31.3.81 but before 1.4.91; (*ii*) a ship acquired by an Indian company after 31.3.81 but before 1.4.91; (*iii*) a hotel owned by an Indian company approved by the Government set up after 31.3.81 but before 1.4.91; and	Co-op. Societies other assessees for 10 years	Non-coporate assessees = 25% of such profit, corporate, assessees—30% of such profit.
15. 80 IA	**Deduction for profits from industrial undertaking, ship or hotel**	All assessees -do- only for Indian companies only for Indian companies	(*a*) Industrial undertaking set up after 1.4.91 but before 31.3.95 (*b*) Industrial undertaking set up in industrially backward areas during 1.4.94 to 31.3.99 (*c*) Industrial undertaking set up in small scale sector during 1-4-91 to 31.3.2000 (*d*) Ship acquired after 1-4-91 but before 31.3.95 (*e*) Business of Hotel set up in rural areas, hilly areas or places of pilgrimage during 1.4.90 to 31.3.94		25% (for all but) 30% (only companies) of profits from such unit for 10 years 30% of profits from shipping business for 10 years. 50% of profits form such Hotel for 10 years

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		only for Indian companies	(f) Business of Hotel set up any where in India during 1.4.91 to 31.3.95		30% of profits from such hotel of 10 years. (In all the above cases deduction is to be allowed for 12 years to a Co-op. Society)
16. 80 JJ	**Profits of Poultry farming**	All assessees	Profits of Poultry farming Business	Every year	33⅓% of profits from Poultry farming
17. 80 L	**Dividend, interest and other such incomes**	Individual & H.U.F. only	(i) Int. on units of U.T.I. (ii) Int. on Bank deposits (iii) Int. on Government securities (iv) Dividend from an Indian Co. (v) Dividend from coop. society (vi) Int. on coop. debentures (vii) Int. on deposits with coop. societies (viii) Int. on Compulsory Deposits Scheme (ix) Int. on deposits with financial corporations (x) Int. on deposits with housing development authorities (xi) Interest on NDS (xii) Interest on debentures of prescribed authority of public sector company	Every year in which such income are included in G.T.I.	Actual total or Rs. 12,000 whichever is less Additional Rs. 3,000 if Dividend from Indian Co. or Interest or Dividend of units of U.T.I. or Mutual Funds is included.
18. 80 O	**Royalty etc. received from foreign companies**	Companies and Resident assessees	For allowing use of patent, invention or technique to a foreign company or concern by an Indian company, any profits which are brought into India in foreign exchange.	-do-	50% of such royalty
19. 80 P	**Income of cooperative societies**	Coop. Society	Profits of coop. society from (a) Banking business (b) Cottage industry (c) marketing of agricultural products (d) agricultural implements, seeds, livestock etc. (e) processing		

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Section	Deduction	Who can Claim	Qualifying Amount	Period	Rate
			(*f*) collective disposal of labour (*g*) fishing and other allied activities (*h*) business of supplying milk, fruits, oil seeds or vegetables (w.e. from 1.4.88) to Govt, or federal coop. society or a Govt institution or statutory corporation	Every year	100% of such profits.
			Profits of a coop. Society from any other activity.	Every year	Rs. 40,000 are allowed as deduction.
			Income from interest or dividend from any other coop. society.	Every year	100% of such
			Income from letting of godowns	Every year	100% such Income.
			Income of a society from transport business & manufacturing business with the aid of power—provided G.T.I. does not exceed Rs. 20,000	-do-	100% of amount of interest on securities or property income
20. 80 R	**Remuneration earned outside India by professors and teachers, etc.**	Indian citizen Individual	Remuneration received outside India for work done in educational institutions.	Every year	75% of remuneration brought in foreign exchange in India.
21. 80 RR	**Professional income from foreign sources**	Resident citizen Individuals	Income from outside India through their professional intelligence, skill or as an author, brought into India in foreign exchange.	In the year in which income is earned.	-do-
22. 80 RRA	**Remuneration received from foreign employers**	Resident citizen Individuals	Salary received from foreign employers	-do-	-do-
23. 80 U	**Medically Handicapped or Mentally retarted assessees**	Resident Individuals	If assessee is blind or medically handicapped and produces a medical certificate.	Every year	Rs. 40,000 p.a.

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Illustration 6. The following are particulars of income of Mr. Behl for the year:

		Rs.
1.	Income from House property	61,200
2.	Business Income	80,000
3.	Dividends (Gross)	200
4.	Long Term Capital Gain: Long Term	
	(*a*) from Land	1,000
	(*b*) from Shares	800

5. He paid Rs. 28,000 as Life Insurance premium on his own life on a policy of Rs. 2,00,000.
6. He gave Rs. 20,000 as donation to a charitable institution approved under section 80G.
7. During the year he deposited Rs. 20,000 in a scheme (Dhan 88) notified u/s 88.
8. He deposited Rs. 12,500 in National Saving Scheme 1992.
9. Interest accrued on N.S. certificates VIII issue purchased in May 1992 for Rs. 20,000 is Rs. 2,780.

Compute his Total Income and amount qualifying for rebate u/s 88.

Solution

Computation of Total Income of Mr. Behl.

	Rs.	Rs.	Rs.
Income from House Property			61,200
Business Income			80,000
Capital Gain: Land		1,000	
Shares		800	
Total Long Term Capital Gain			1,800
Other sources: NSC VIII issue Interest		2,780	
Dividend		200	
			2,980
Gross Total Income			1,45,980
Deductions u/s 80			
(*i*) u/s 80 L: Dividend	200		
Int. on NSC VIII issue	2,780		
		2,980	
(*ii*) u/s 80 G: Donations			
Q.A. Actual Donation Rs. 20,000 or			
10% of G. Tax I w.e. is less			
10% of [1,45,980 – (2,980 + 1,800] = 14,120			
Rate 50% of Rs. 14,120		7,060	
			10,040
Total Income			1,35,940

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Q.A. for Rebate of tax u/s 88	Rs.
(*i*) Life Insurance Premium	28,000
(*ii*) Interest on NCS VIII issue	2,780
(*iii*) Amount deposited in NSS 1992	12,500
(*iv*) Amount invested in Dhan 88 (Maximum)	10,000
Total Qualifying Amount	53,280

Illustration 7. Sh. S.K. Basu is in service in Calcutta drawing a monthly salary of Rs. 5,000 p.m. He is also provided with a free unfurnished flat, the rent of which is Rs. 1,000 per month. He contributes 10 per cent of his salary to a recognised provident fund. The interest on his Provident Fund Account for the year ended 31st March 1997 amounted to Rs. 250. He is also the owner of a house which is let out at a monthly rent of Rs. 2,500. His expenses for house were:

	Rs.
(*a*) Municipal taxes	3,000
(*b*) Interest on loan for construction of the house	6,600
(*c*) Repairs	500

He has also received dividend on investments amounting to Rs. 12,000 (Gross).

He has also received a share from a firm assessed as firm of Rs. 5,000 and his share of registered firm's tax amounts to Rs. 600. He has paid life insurance premium for a policy on his own life Rs. 700. He paid Rs. 200 to P.M. National Relief Fund.

Compute the Total Income of Shri Basu. *[Nagpur. M.Com.]*

Solution

Computation of Total Income of Shri S.K. Basu.

		Rs.	Rs.
I. *Salary:*			
Salary @ 5,000 p.m.		60,000	
Perquisite: Rent-free unfurnished flat—			
10% of salary =	6,000		
Add: F.R.V. (–) 60% of salary (12,000 – 36,000)	Nil	6,000	
Total Salary		66,000	
Less: Standard Deduction u/s 16 (i) $33^1/_3\%$ of 66,000 or Rs. 15,000 w.e. is less		15,000	
Salary Income			51,000
II. *House Property:*			
Annual rental value: @ Rs. 2,500 p.m.		30,000	
Less: Taxes		3,000	
Annual value		27,000	

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Deductions:	Rs.		
(*a*) 1/5th for repairs	5,400		
(*b*) Interest on Loan for construction of house	6,600		
		12,000	
			15,000
III. *Business or Profession:*			
Share from firm assessed as firm (Exempted u/s 10(2A)]			Nil
IV. *Other Sources:*			
Dividend (Gross)			12,000
Gross Total Income			78,000
Deductions: u/s 80 L : Dividend		12,000	
80 G : Donation to P.M. Relief Fund		200	
			12,200
Total Income			65,800
Rebate u/s 88: Q.A.			
Contribution to R.P.F. @ 10% of salary		6,000	
Life Insurance Premium		700	
Q.A.		6,700	

Illustration 8. You are required to compute total taxable income of Mr. Kapoor for the financial year ending 31st March, 1997 from the following particulars:

(*a*) Salary per month Rs. 4,000. He spent 3 months in Australia on leave on full pay. On 31st Dec. he was discharged on payment of a compensation of Rs. 9,000. Salary accrues on the last date of the month.

(*b*) He contributed towards Provident Fund (Recognised) at 15 per cent of his salary. Similar amount was contributed by his employer. He paid Rs. 4,000 on the assurance of his own life.

(*c*) He held Rs. 1,00,000, 10 per cent Govt. of India Loan 1999. He paid an interest of Rs. 7,000 on a loan which he look for the purchase of such investment.

(*d*) He owns several properties in Calcutta the rental value of which amounts to Rs. 86,800 per annum including Rs. 11,800 for a cottage where he resides. He has incurred the following expenses: Vacancy Allowance Rs. 2,400, Repairs Rs. 14,000, Collection Charges Rs. 6,000, Legal Charges for acquisition of land Rs. 20,000.

(*e*) He had also some agricultural land in Nepal and he derived an income of Rs. 10,000.

(*f*) He also received 1/5th share from Hindu Undivided Family Rs. 15,000.

(*g*) He is medically handicapped person and has been duly certified by the Govt. doctor.

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(*h*) He paid Rs. 4,000 as premium under the scheme of Mediclaim for insurance of his health and health of all his family members.

Solution

Computation of Total Income of Mr. Kapoor for the current assessment year.

		Rs.	Rs.
Income from Salary			
Salary @ Rs. 4,000 p.m. (1.4.96 to 31.12.96) (9 months including leave salary)		36,000	
Compensation on termination of service		9,000	
Employer's Contribution in Employee's R.P.F. over 10% of salary (5,400 – 3,600)		1,800	
Gross Salary		46,800	
Less: Standard deduction u/s 16 (i) Maximum		15,600	
			31,200
Income from House Property:			
Let-out House Property:			
Rental value (86,800 – 11,800)		75,000	
Less: Municipal Taxes		—	
Net Annual Value		75,000	
Deductions:			
	Rs.		
1/5th of A.V. as repairs	15,000		
Vacancy allowance	2,400		
		17,400	
			57,600
Self-occupied House: Annual value is taken as			Nil
Income from other sources:			
Agricultural Income from Nepal		10,000	
Interest on Govt. Loan	10,000		
Less: Interest on Loan paid	7,000		
		3,000	
			13,000
Gross Total Income			1,01,800
Deductions u/s 80			
(*i*) *u/s 80 L:* Interest on Govt. Loan		3,000	
(*ii*) u/s 80 D: Premium paid to Mediclaim (Actual Rs. 4,000 or Rs. 6,000 w.e. is less)		4,000	
(*iii*) u/s 80 U: Medically Handicapped assessee		40,000	
			47,000
Total Income			54,800
Rebate of tax u/s 88: Q.A.			
Contribution to R.P.F.	5,400		
L.I.C. premium	4,000		
Q.A.	9,400		

Note: Share of Income received from H.U.F. is exempted from tax u/s 10(2).

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Illustration 9. Compute assessable income of Mr. C.L. Arora residing in Bombay, for the current assessment year as per details given below:

		Rs.
(*i*)	Salary (Non-Govt. employee)	45,000
(*ii*)	Entertainment allowance (Before 1.4.55 he was not getting any E.A.)	10,000
(*iii*)	Bonus	3,180
(*iv*)	Dearness allowance (Not includible for retirement benefit)	4,800
(*v*)	Employer's contribution to Recognised Provident Fund	2,800
(*vi*)	Additional dearness allowance	1,200
(*vii*)	Club Bill (paid by employer)	500
(*viii*)	Car expenses (Including Dep.) (own car:18 HP: used for the purposes of employment)	7,600
(*ix*)	Rent-free furnished accommodation provided by employer (valued unfurnished)	10,000
	(Cost of furnishing)	30,000
(*x*)	Medical expenses met by employer	1,000
(*xi*)	Reimbursement of Hotel Bill	240
(*xii*)	Employee's contribution to Provident Fund (Recognised)	2,800
(*xiii*)	Life Insurance Premium (sum assured) Rs. 50,000	8,000
(*xiv*)	Purchase of books (necessary for Employment)	430
(*xv*)	Investment in Debentures of A Ltd. (Rate of interest 8%)	60,000
(*xvi*)	Municipal Value of house at Calcutta, construction started in Jan. 1983 and completed on 31st *July 1991*	34,200
(*xvii*)	Actual rent received from both the units	38,400
(*xviii*)	Fire Insurance Premium paid	1,165
(*xix*)	Interest paid on capital borrowed for construction of house	8,000
(*xx*)	Collection charges paid	2,400
(*xxi*)	Municipal Taxes paid	4,000
(*xxii*)	Short Term Capital Gain	5,000
(*xxiii*)	Long Term Capital Gain	20,000
(*xxiv*)	Income from Dividend (Gross)	3,000
(*xxv*)	Interest on 9% (Tax free) Power Finance Corporation of India Bonds	2,000
(*xxvi*)	He paid Rs. 5,000 to Burdwan University for Scientific Research	
(*xxvii*)	He invested Rs. 7,500 in G.I.F.T. (a notified scheme of mutual fund under equity linked saving scheme)	
(*xxviii*)	For completion of house property, a loan was taken from HDFC. The principal amount repaid to HDFC was @ Rs. 1,000 p.m. and interest of Rs. 4,000 (claimed as deduction as per (*xix*) above).	

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Solution

Computation of Total Income of Mr. C.L. Arora

		Rs.	
I. *Salary:*			
Salary		45,000	
Bonus		3,180	
Dearness allowance		4,800	
Entertainment Allowance		10,000	
Additional dearness allowance		1,200	
Perquisites:			
(*i*) Rent-free furnished Accommodation:			
Annual rental value of unfurnished house = Rs. 10,000			
10% of salary (45,000 + 3,180 + 10,000 = 58,180)	5,818		
Add: Excess of F.R.V. *over* 60% of salary (10,000 – 34,908)	NIL		
Add: 10% of cost of furnishing *i.e.*, 10% of 30,000	3,000		
	8,818		
(*ii*) Club Bills	500		
(*iii*) Hotel Bill	240		
		9,558	
Gross Salary		73,738	
Standard Deduction u/s 16(i) (Maximum)		15,000	
Salary Income			58,738
II. *Income from House Property:*			
Annual rental value		38,400	
Less: Municipal taxes		4,000	
		34,400	
Less: New Construction allowance @ Rs. 3,600 per unit for two units for four months each		2,400	
Net Annual Value		32,000	
Deductions:	Rs.		
1/5th for repairs	6,400		
Fire Insurance premium	1,165		
Interest on capital borrowed for construction	8,000		
		15,565	
Income from House Property			16,435
III. *Capital Gains:*			
Short-term		5,000	
Long-term Capital Gain (Land)		20,000	
			25,000

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IV. *Income from Other Sources:*		
Dividend	3,000	
Interest on 60,000, 8% Debentures	4,800	
		7,800
Gross Total Income		1,07,973
Deductions u/s 80		
(*i*) *80 GGA:* Amount given to university for scientific research @ 100%	5,000	
(*ii*) *80L:* Dividend	3,000	
		8,000
Total Income		99,973

(Rounded off to Rs. 99,970)

Rebate of Tax u/s 88: Q.A.

Life Insurance Premium	8,000
Contribution to Recognised P.F.	2,800
Repayment of loan taken from HDFC (Restricted to Rs. 10,000)	10,000
Amount invested in GIFT	7,500
Qualifying Amount	28,300

Note: (*i*) Reimbursement of Medical expenses is tax-free perquisite.

(*ii*) Interest on 9% (Tax free) Bonds of power Finance Corporation is exempted u/s 10(15).

Illustration 10. Discuss the chargeability to income-tax or otherwise of following items:

(*a*) Dividends received by a shareholder from a company out of its agricultural income.

(*b*) Sales-tax collected by an auctioneer.

(*c*) Compensation received for termination of employment.

(*d*) Moneys and assets received on partition of Hindu Undivided Family.

(*e*) Loans received by a director of a closely held company from another company.

Solution

(*a*) Dividend paid by a company to its shareholders out of its agricultural income is not income derived from land since the immediate and effective source of dividend income to the shareholder is the shareholding in the company and not the land. *[Bacha Guzdar v. C.I.T.]*

(*b*) The amount of sales tax is collected from the buyer and is included in the amount of the sales and hence is chargeable to tax as income from business u/s 28. The treatment given by the auctioneer in his books of accounts is totally immaterial for the purpose. The consideration that the auctioneer is not the owner of his goods is also immaterial.

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(*c*) Although it is a capital receipt yet it is taxable as salary income u/s 17(3) subject to exemption u/s 10(10B) and it is known to be a profit in lieu of salary.

(*d*) Moneys and assets received by a coparcener at the time of partition of the H.U.F. do not constitute a receipt which is chargeable to tax in his hands.

(*e*) Loan received from another company does not constitute a dividend u/s 2(22).

Q. No. 9

Mr. Mahapatra, a physically handicapped assessee submits following particulars of income for the year ended 31.3.1997—

(*i*) Rent from house at Calcutta Rs. 24,000 p.a. Municipal Taxes paid by tenant Rs. 1,200 which is 50% of total taxes. HP was completed on 1.11.91

(*ii*) Poultry farming business income Rs. 61,000

(*iii*) Speculation gain from shares Rs. 20,000
Speculation loss from Gold Rs. 30,000

(*iv*) Other sources—

(*a*) Dividend from Indian company	Rs. 9,000
(*b*) Interest on units of Mutual Fund	Rs. 2,000
(*c*) Bank Interest	Rs. 5,000
(*d*) Interest on debentures	Rs. 33,000

(*v*) He paid Rs. 10,000 to a veterinary college of Bengal Govt. engaged in research in poultry farming.

(*vi*) He gave Rs. 6,000 to Calcutta Municipal Corporation for carrying out a project approved by National Committee.

Calculate his total income and advise him about the amount which he should deposit is National Saving Scheme 1992 so that his tax liability for the assessment year 1997-98 is NIL.

[**Hints**: HP Income Rs. 16,560 (NCA from 7 months) *P & G* Rs. 45,000 speculation loss to be C/F other sources Rs. 49,000 GTI Rs. 1,10,560 Deduction u/s 80 JJ Rs. 15,000 u/s 80L 15,000 u/s 80 U Rs. 40,000 Total income Rs. 40,560 Amount to be deposited in NSS Rs. 420] [P-26]

Q. No. 10

An assessee, who is an individual received the following incomes during the financial year 1996-97 :—

	Rs.
(*i*) Insurance commission received from L.I.C.	10,656
(*ii*) Cloth Business Profits	75,000
(*iii*) He made the following payments during the year :	
(*a*) Deposit of Rs. 10,000 in National Saving Scheme 1992.	
(*b*) Payment of Rs. 500 p.m. to Jeevan Dhara Policy.	

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(*c*) Investment of Rs. 20,000 in units of mutual funds so notified u/s 88.

(*d*) Donation given to

	Rs.
National Children Welfare Fund	5,000
P.M. National Relief Fund	5,000
P.M. Africa Relief Fund	2,000
P.M. Folks Arts Fund	1,000
P.M. Students' Aid Fund	2,000
Maharashtra C.M.'s Earthquake Relief Fund	2,000
Local authority to promote Family Planning	2,000
Public Charitable Trust (Approved)	10,000

(*vi*) He paid Rs. 6,000 by cheque to General Insurance Company under Medi claim.

Compute his total income and qualifying amount for rebate u/s 88.

[Panjab B.Com. Oct. 1995]

[**Hints :** Total Income Rs. 59,799; Q.A. for rebate Rs. 26,000 Deduction u/s 80D, Rs. 6,000 80G Rs. 16,305 Ad hoc deduction for 1/3 commission from L.I.C.] [P-27]

Q. No. 11

The following are the particulars of the income of a professor of a University:

(*i*) Salary Rs. 5,400 p.m. from which 10% is deducted for provident fund to which university also contributes 12%.

(*ii*) Wardenship allowance Rs. 1,200 p.a.

(*iii*) Rent-free bungalow of which the annual letting value is Rs. 6,000.

(*iv*) 8% dividend on 50 shares of Rs. 100 each in a Limited Company.

(*v*) 10% interest on Government Loan of Rs. 5,000.

(*vi*) Income from interest on Postal Saving Bank Deposits Rs. 500.

(*vii*) Income from property let, Rs. 7,200 (Computed).

(*viii*) Profit on sale of property, Rs. 1,500.

(*ix*) Income from royalty on copyright of his work, Rs. 2,000.

(*x*) Examinership remuneration, Rs. 3,700.

(*xi*) He paid Rs. 10,000 as donation to Family Planning Association of India.

During the year, he paid Rs. 3,950 as life insurance premium of which Rs. 500 was paid on a joint life policy. He also purchased books worth Rs. 650 during the same year. He maintains a scooter for going and coming from the University.

Find out his total income and exempted income. *[Guru Nanak B.Com.]*

[**Hints :** Salary Income Rs. 57,000; House Property Rs. 7,200, S.T. Capital Gain Rs. 1,500; other sources Rs. 6,600, G.T.I. Rs. 72,300, Deduction u/s 80L Rs. 900, u/s 80G Rs. 7,140 Total Income Rs. 64,260 Q.A. for rebate u/s 88 Rs. 10,430] [P-3]

Q. No. 12

A, who is a lecturer in a College, is getting a salary of Rs. 2,500 per month plus 23% of salary as dearness allowance. He contributes 10% of his salary to a provident fund to which the college contributes an equal amount. He is also a hostel warden and is provided with rent-free quarters the annual rental value of

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which is Rs. 1,600. He owns a bungalow which is let out for Rs. 200 per month and for which he pays municipal taxes amounting to Rs. 300 per annum.

During the year ended 31st March, 1997 he earned the following incomes:

(*i*) 15 per cent dividend on shares of Rs. 15,000 in the Hindustan Chemicals Ltd.

(*ii*) Received Rs. 30,000 as Panjab State Lottery.

(*iii*) 10% interest on Rs. 18,000 invested in Government Securities.

(*iv*) 9% interest on debentures of Rs. 15,000.

(*v*) Rs. 1,505 as dividend on the units of Unit Trust of India. He has insured his life for Rs. 25,000 and paid Rs. 1,250 by way of premium on his life policies during the year ended 31st March, 1997.

(*vi*) Mr. A paid Rs. 6,000 to Punjab University Chandigarh for research in the field of bio-sciences.

You are required to ascertain his Total Income. *[Kurukshetra, B.Com.]*

[**Hints:** Value of Rent-free House Rs. 1,600; Salary Income Rs. 25,667; House Property Rs. 1,680; Other sources Rs. 51,905; Deduction u/s 80L Rs. 5,555; u/s 80GGA Rs. 6,000 Total Income Rs. 67,697. Q.A. for Rebate u/s 88 Rs. 4,250] [P-28]

Q. No. 13

Compute the total income of Shri R. Shankar who is working as Sales Manager of Z Co., Ltd., Bombay, for the current assessment year. He received the following incomes and perquisites in the accounting year:

(*i*) Salary	Rs. 3,000 p.m.
(*ii*) Dearness Allowance, as per terms of employment, it is included into computation of service benefits	Rs. 600 p.m.
(*iii*) Employer's contribution to Recognised Provident Fund; Shri R. Shanker also contributes a like amount each month	Rs. 400 p.m.
(*iv*) Interest credited on Shri R. Shanker's balance in the Provident Fund @ 11% p.a.	Rs. 2,400
(*v*) Entertainment Allowance Granted Regularly since 1954	Rs. 7,400
(*vi*) Rent-free unfurnished accommodation. Rent paid by the employer	Rs. 800 p.m.
(*vii*) Free use of a 20 H.P. motor car; Running and maintenance expenses wholly incurred by employer	Rs. 12,800
(*viii*) Dividends from a co-operative society (Gross)	Rs. 1,200
(*ix*) He received Rs. 2,700 as interest on units of U.T.I. and dividend from Indian Company Rs. 8,000 (after deduction of tax @ 20%)	
(*x*) He invested Rs. 6,000 in CANPEP (a notified equity linked deposit scheme)	

Shri R. Shanker was resident for the previous year and he paid Rs. 3,500 as insurance premium on a policy of Rs. 30,000 taken on his life.

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[**Hints:** Value of rent-free house Rs. 4,340; Gross Salary Rs. 68,220: Deduction u/s 16(i) Rs. 15,000 and u/s 16(ii) Rs. 7,200; Salary Income Rs. 46,020; Other sources Rs. 13,900; G.T.I. Rs. 59,920; Deduction u/s 80L Rs. 13,900; Total Income Rs. 46,020; Q.A. for Rebate u/s 88 Rs. 14,300] {P-29]

Q. No. 14

Shri S. Rath, a resident individual, is an executive of an Indian company at Cuttack. For the year, he furnished the following particulars of his income:

(*a*) Net salary drawn Rs. 42,000

(*b*) Tax deducted at source Rs. 4,400

(*c*) Provident fund deducted and credited in the Recognised Provident Fund Rs. 4,200

(*d*) Perquisites enjoyed:

- (*i*) Free furnished accommodation at Cuttack, the fair rent of which Rs. 500 per month and rent paid by the employer for furniture Rs. 50 per month;
- (*ii*) Employer paid life insurance premium on Shri Rath's life policy Rs. 1,500 which is less than 10% of the sum assured;
- (*iii*) A 12 H.P. motor car for Shri Rath's use for office and personal purposes. Expenses met by employer.

(*e*) Shri Rath's Bank A/c shows the following credits: Total interest Rs. 440 and a sum of Rs. 2,500 as Profit Bonus received during the year. Interest on units of Mutual Fund Rs. 10,000.

(*f*) Shri Rath further declares that his payment of life insurance premium on a joint life policy with his wife being Rs. 2,240 on the capital sum assured Rs. 20,000.

(*g*) Ten-year cumulative time deposit Rs. 2,400.

(*h*) Mr. Rath paid

- (*i*) Rs. 3,000 by cheque as medical insurance premium to G.I.C. for assuring the health of his family members,
- (*ii*) Rs. 2,000 in cash as premium under Mediclaim for his dependent father.

Compute the taxable income.

[**Hints:** Salary Income Rs. 52,710; Other sources Rs. 10,440; G.T.I. Rs. 63,150; Deduction u/s 80L Rs. 10,440 u/s 80D Rs. 3,000 Total Income Rs. 49,710; Q.A. for rebate u/s 88 Rs. 10,340] [P-4]

Q. No. 15

Mr. A.B., General Manager of Modern Products Ltd., is in receipt of a salary of Rs. 3,000 p.m. and an entertainment allowance of Rs. 500 p.m. (The allowance was increased to this rate from 1st April, 1970 and he had been getting Rs. 400 p.m. for eighteen years before that date). He is in occupation of a fully furnished house for which the company pays rent of Rs. 900 p.m. to the landlord. It does not recover anything from Mr. A.B. for the personal use of a big car, and the pay of the chauffeur and running expenses, repair charges etc. are fully met by the company. Estimated expenditure incurred by employer on big car is Rs. 6,000 p.a. The company also maintains a Recognised Provident Fund to which Mr. A.B. contributes Rs. 500 p.m. and the company contributes an equal amount. Interest credited to the fund (at the rate of 8% p.a.) is Rs. 1,500. During the year ended 31st March 1997. Mr. A.B. also has the following incomes:

Rent of a house let out at Rs. 8,000 p.m. (Municipal Taxes Rs. 9,600 per year).

Gross dividends Rs. 8,000.

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He pays life insurance premia of Rs. 6,000 a year. Mr. AB went to Calcutta to attend one year course during 1994-95 and took a loan of Rs. 1,50,000 for this purpose. During 1996-97 he repaid Rs. 30,000 towards principal amount and Rs. 10,000 as interest.

Calculate his Total Income and indicate the deductions to which he is entitled.

(Guru Nanak, B.Com.)

[**Hints:** Salary Income Rs. 27,280, House Property Rs. 69,120, Other sources Rs. 8,000 G.T.I. Rs. 1,04,400 Deduction u/s 80E Rs. 25,000 and u/s 80L Rs. 8,000 Total Income Rs. 71,400.] [P-5]

Q. No. 16

Mr. Bhaskar Rao, General Manager of Atul Products Ltd., is in receipt of salary of Rs. 5,500 per month. He is in occupation of an unfurnished house for which the company pays a rent of Rs. 800 per month to the landlord but does not recover anything from Mr. Bhaskar Rao. The company also maintains a recognised provident fund to which Mr. Rao contributes Rs. 9,000 per annum and the company contributes an equal amount. Interest credited to the Fund is Rs. 9,500 (at the rate of 10% per annum). During the year ended on 31st March, 1997 Mr. Rao also has the following incomes:

(*i*) Rent of a house (built in 1956) let out at Rs. 800 per month (Municipal Taxes Rs. 2,100 per annum).
(*ii*) Gross dividends Rs. 3,000.
(*iii*) Bank Interest Rs. 4,000.
(*iv*) Interest on debentures Rs. 6,000.
(*v*) Interest on N.S.C. VIII issue (Accrued) Rs. 3,000.
(*vi*) Donation given to Zila Saksharata Samiti Rs. 8,000.

He pays life insurance premia of Rs. 4,000 a year on his own life, on a policy of Rs. 45,000.

He maintains a car for his office and family use. Calculate his total income for the assessment year 1997-98 and indicate the deductions to which he is entitled.

[**Hints:** Salary Income Rs. 60,000; House property Rs. 6,000; Other sources Rs. 16,000; G.T.I. Rs. 82,000. Deduction u/s 80L Rs. 10,000; u/s 80G Rs. 8,000; Total Income Rs. 64,000; Q.A. for rebate u/s 88 Rs. 16,000] [P-30]

Q. No. 17

Mr. A is the Managing Director of a Private Limited Co. From the following particulars furnished to you by him, please compute the total income of Mr. A for the assessment year 1997-98:

		Rs.
(*i*)	Salary from the Company	84,000
(*ii*)	Dividend (gross)	6,000
(*iii*)	Sitting Fees	500
(*iv*)	Company's contribution to a recognised provident fund	9,000
(*v*)	Interest allowed on provident fund to Mr. A @ 12%	3,000
(*vi*)	Mr. A contributed to the provident fund	9,000
(*vii*)	Conveyance allowance received from the Company (the car belonged to him which was used for employment purposes also and full amount is spent)	2,500
(*viii*)	Medical expenses of Mr. A paid by the Company	2,000
(*ix*)	The company provided a furnished rent-free bungalow. The Municipal valuation of the bungalow is Rs. 1,200 p.m. Rent of Furniture paid by Co. is Rs. 300 p.m.	

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(*x*) Life insurance premium paid by Mr. A on the life of his wife 5,600

(*xi*) Amount paid in Cash Rs. 2,000 and by cheque Rs. 4,500 as premium for health insurance under notified scheme of Mediclaim for his dependent mother and own family respectively.

The reasons of inclusion or exclusion of the different items should be briefly indicated. *[Kurukshetra, B.Com.]*

[**Hints:** Value of rent-free accommodation Rs. 12,000; Salary Rs. 81,600; Income from other sources Rs. 6,500; G.T.I. Rs. 88,100; Total Income Rs. 77,600 Q.A. for rebate u/s 88 Rs. 14,600] [P-31]

Q. No. 18

From the following facts compute the total income of Shri Ashwani Kumar, General Manager of Diya Limited. His previous year ended on 31.3.1997.

		Rs.
(*i*)	Salary	30,000
(*ii*)	Dearness allowance	5,000
(*iii*)	Bonus	8,000
(*iv*)	He received house rent allowance from the employer—actual rent paid by him was Rs. 6,000.	3,750
(*v*)	In April 1996, he received 50 bonus shares on his original holding of 100 equity shares of face value Rs. 10 each, purchased at Rs. 15 per share four years ago. He sold 50 bonus shares during the year @ Rs. 20 each.	
(*vi*)	He received dividends on units from U.T.I.	1,800
(*vii*)	Received interest on Bank deposits	4,000
(*viii*)	He owns a house with annual rental income	12,200
	He incurred the following expenses:	
	Local tax	1,000
	Ground rent	247
	Interest paid on loan taken for construction	1,000
	The house was completed on 31.3.1992.	
(*ix*)	He deposited Rs. 5,000 in N.S.S. 1992 and Rs. 1,800 in C.T.D. A/c in the Post Office during the year and paid life insurance premium amounting to Rs. 3,500 on sum assured of Rs. 30,000.	

[Company Secretaries, Final]

[**Hints:** Deduction u/s 16(i)—Rs. 14,583 Salary income Rs. 29,167, House Property Rs. 4,833. Other sources Rs. 5,800; Short Term Capital Gain on the sale of Bonus shares Rs. 1,000, G.T.I. Rs. 40,800, Deduction u/s 80L Rs. 5,800. Total Income Rs. 35,000 Q.A. for rebate u/s 88 Rs. 10,300] [P-11]

Q. No. 19

Mohanram, managing director of F.F. Ltd., has furnished the following details for the financial year ended 31 March:

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(*i*) He has been receiving a salary of Rs. 6,000 per mensem. The company is contributing Rs. 500 every month towards his recognised provident fund which is equal to his own contribution.

(*ii*) The company has taken out a life insurance policy of Rs. 40,000 on his life. A monthly premium of Rs. 500 is paid by the company. The company has no beneficial interest in the policy.

(*iii*) He has won a prize of Rs. 20,000 on 31.10.1996 on a Tamil Nadu Government Lottery Ticket.

(*iv*) He has purchased on 1.6.1990 shares of certain companies for Rs. 40,000 on investment account. These shares were sold on 20.3.1997 for Rs. 95,000. *[C.I.I. for 1990-91 is 182 and for 1996-97 is 305]*

(*v*) A dividend @ 15% was received on the face value of Rs. 40,000 of the shares mentioned in item No. (*iv*) above.

(*vi*) A sum of Rs. 10,000 was received from Mauritius University for a lecture assignment on fibres. He brought whole of this income in foreign exchange in India.

(*vii*) He donated blankets worth Rs. 4,000 to an approved Flood Relief Fund.

(*viii*) He resided in his own bungalow. The monthly letting value was Rs. 1,200 whereas its municipal rental value is Rs. 16,200 p.a. The annual expenses on municipal taxes and repairs amounted to Rs. 3,000 and Rs. 6,000 respectively.

Please assist the Managing Director in preparing his income-tax return for the assessment year 1997-98.

[**Hints**: Income from salary 63,000. House property—NIL; Capital Gains—Rs. 27,967; Income from other sources Rs. 31,000; G.T.I.—Rs. 1,21,967; Deduction u/s 80RRA 7,500 and 80L Rs. 6,000; Total Income—Rs. 1,08,467 Q.A. for rebate u/s 88 Rs. 12,000] [P-12]

Q. No. 20

Mr. A received the following incomes during the year ended on 31st March.

	Rs.
(*a*) Salaries from his employers @ Rs. 3,000 per month	33,000
(*b*) Leave Travelling Allowance for proceeding on leave to home district in India	4,000
(*c*) Lunch Allowance @ Rs. 250 per month	2,750
(*d*) Reimbursement of medical expenses from employers	4,700

Mr. A also enjoyed the following other benefits and perquisites:

(*a*) Free unfurnished flat in Bombay for which his employers were paying a rent of Rs. 1,200 per month.

(*b*) One free car of 14 H.P. with driver for personal use. Mr. A had certain investments in shares on which he earned dividends of Rs. 8,000. Out of this, however, only Rs. 6,100 were received in hand after deducting tax at source of Rs. 1,800 and bank commission of Rs. 100 paid to Bank for realising the dividend.

Mr. A's salaries and allowances due on 31st March, 1997 which remained unchanged, were received by him only in April 1997.

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Compute the Gross Total Income of Mr. A (ignoring deductions from Total Income) for the year ended on 31st March, 1997. *[Adapted C. A. (Inter)]*

[**Hints:** Salary due for the month of March is taxable in the current previous year, Salary Income—Rs. 35,800; Income from other sources—Dividend Rs. 7,900 (*i.e.* Rs. 8,000—Bank Commission of Rs. 100) G.T.I.—Rs. 43,700] [P-13]

Q. No. 21

Smt. Surekha, Company Secretary of M/s Dinesh Dye Stuff Industries Private Limited, furnished the following particulars of her total income relevant to the previous year ended 31.3.1997. You are required to compute the total income of Smt. Surekha for assessment year 1997-98.

		Rs.
(*i*)	Salary	42,000
(*ii*)	Dearness allowance	7,000
(*iii*)	Bonus	5,000
(*iv*)	Salary in lieu of leave	3,500
(*v*)	Reimbursement of ordinary medical expenses	1,200
(*vi*)	Payment of club bills (including entrance fee of Rs. 2,500 and annual subscription of Rs. 500 to Rajpath Club Ltd.) by employer	3,000
(*vii*)	Bank interest	5,000
(*viii*)	Dividend (Gross)	3,000
(*ix*)	Unit Trust Dividend	3,000
(*x*)	Agency Commission earned	5,000
(*xi*)	Interest credited in Public Provident Fund Account	1,500
(*xii*)	She has earned Rs. 10,000 long-term capital gain on sale of her personal jewellery which she inherited from her mother in 1981.	
(*xiii*)	L.I.P. payments—	Rs.
	on own life	2,000
	on major son's life	1,000
	on major daughter's life	500
(*xiv*)	Contribution to Public Provident Fund Account	2,000
(*xv*)	She has taken Unit Linked Insurance Policy and contributed	1,000
(*xvi*)	Contribution to R.P.F.	5,500
(*xvii*)	Payment of fees to her husband Shri M.C. Shah (Practising Chartered Accountant) for preparing her income-tax return and appearing before the Income Tax Authority	500
(*xviii*)	Donation to Sarvodaya Medical Society—its programme of rural development has been approved u/s 35 CCA by the Income Tax Authority	5,000
(*xix*)	She made investment in certain units of mutual fund which are eligible for rebate under equity linked saving scheme	5,000
(*xx*)	She deposited Rs. 5,000 in National Savings Scheme.	

[Company Secretaries (Final)]

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[**Hints:** Standard deduction Rs. 18,000; Salary Income Rs. 42,500; L.T. Capital gain Rs. 10,000; Other sources Rs. 16,000; G.T.I. Rs. 68,500; Deduction u/s 80L Rs. 11,000; 80 GGA Rs. 5,000; Total income Rs. 52,500 Q.A. for rebate u/s 88 Rs. 22.000] [P-14]

Q. No. 22

Das is the General Manager of Eros Co. Ltd., Delhi since April 1965. He draws a salary of Rs. 4,000 p.m. and is in occupation of a rent-free accommodation (unfurnished) given by the company, the fair rent of which is Rs. 1,500 p.m. The company also pays him Rs. 300 p.m. as conveyance allowance, Rs. 300 p.m. as entertainment allowance and Rs. 400 p.m. as special pay.

According to the terms of employment the company has to pay him a commission of 1/4% on the net profit of the company. The net profit for the year ended on 31st March is Rs. 40,00,000. Das is a member of the company's R.P.F. to which he and the company contribute Rs. 500 p.m. each. During the year ended on 31st March, Das paid Rs. 500 p.m. on a policy of insurance on his own life for Rs. 50,000. He has also paid Rs. 900 for purchase of books, Rs. 800 as professional tax and Rs. 600 p.m. towards the maintenance of the car owned by him and used equally for office as well as personal purpose.

Das' other incomes for the year are Rs. 6,000 each as dividends (gross) from an Indian and another foreign company; Rs. 1,800 as gross interest on Debentures of Eros Ltd.; Rs. 15,000 as profit on sale of his shop which was let upto 31.3.1996 and was acquired in 1981.

Compute Das's taxable income. *[Adapted Company Secretaries (Final)]*

[**Hints:** Salary income Rs. 58,440 (Value of rent-free accommodation Rs. 6,640; Deduction of Professional Tax Rs. 800); Capital gains Rs. 15,000. Income from other source Rs. 13,800. G.T.I. Rs. 87,240; Deduction u/s 80L Rs. 6,000; Total Income Rs. 81,240 Q.A. for Rebate of tax u/s 88 Rs. 12,000] [P-32]

Q. No. 23

Dr. Sharma, an Indian citizen and a senior professor of Economics in a Government College in India, was posted as Economic Advisor to the Indian Embassy at Washington for a period of three years commencing from 1st April, 1996. Under the terms of employment, he was to receive from the Government, a salary of Rs. 60,000 p.a., house rent allowance of Rs. 1,000 p.m. and the actual fare by air from Bombay to Washington which amounted to Rs. 7,500 only, and was to be paid to him when he reached there. He remained in Washington throughout the year ended on 31st March, 1997 and never came to India in that year.

During this period, he was sending Rs. 1,000 per month to his family for their maintenance and deposited his savings at the average rate of Rs. 500 per month in bank of Washington. The interest credited to his account on 31st March, 1997 was Rs. 480.

He was also provided with a free car by the Government which he used both for personal and office purposes.

During the previous year 1996-97 he had the following other incomes which were deposited to his bank account in India as per his instructions:

Examinership Rs. 2,500.

Royalty on a book which he completed in 18 months Rs. 9,000. He claims 25% of royalty as expenditure.

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He had residential house in India, half of which was let out and half was used by his family. Rent received amounted to Rs. 300 per month. Municipal taxes paid during the year Rs. 800. He paid Rs. 2,200 as life insurance premium.

Compute Dr. Sharma's Total Income for the assessment year 1997-98.

[M.Com., B.H.U.]

[**Hints:** Sharma is non-resident. Salary Income Rs. 42,000; House Property: Rs. 2,560; Other sources Rs. 9,250; Total Income Rs. 53,810 Q.A. for Rebate u/s 88 Rs. 2,200; Interest on deposit in Bank in U.S.A.—exempted] [P-8]

Q. No. 24

Mr. Ramesh, an employee of a rubber plantation in South India, furnishes the following particulars concerning his assessment relevant to the previous year ended on 31st March, 1997:

Basic salary Rs. 2,000 per month; Dearness Allowance, 50% of basic salary according to the terms of employment; enters into pay for service benefits; Marriage allowance Rs. 600 per month; Children's education allowance Rs. 200 per month; Bonus 3 months' salary *i.e.* Rs. 6,000; Entertainment allowance—he has been in receipt of an equal amount of allowance since 1952, Rs. 1,200 per month.

Own contribution to a Recognised Provident Fund at 10% of salary inclusive of dearness allowance; employer's contribution to the said Recognised Provident Fund at $12^1/_2$% of salary inclusive of dearness allowance, Employer's contribution to an approved Superannuation Fund at $7^1/_2$ of basic salary, and interest at 8% on the balance in the Provident Fund Rs. 2,500. Mr. Ramesh has a car of his own which he uses for personal purposes as well as for purposes of his employment. His employer meets the entire cost of maintaining and running for private use of car which are Rs. 2,400 p.a.

Mr. Ramesh is the owner of house property in Madras which remains vacant unless he occupies it when he is in Madras on leave. During the year he stayed there for two months only. The annual value of the property is Rs. 12,000. He took a loan mortgaging the property on which the interest for the year amounted to Rs. 2,400. There were no other expenses in regard to this property except on repairs Rs. 3,000. He is provided with rent-free unfurnished accommodation inside the plantation, the fair rental value of which is Rs. 2,500 p.m. He is required to give up his right of occupation for any period during which he is on leave.

Mr. Ramesh paid life insurance premium of Rs. 12,000, Rs. 4,000 and Rs. 1,000 on three policies of Rs. 1,00,000, Rs. 50,000 and Rs. 20,000 on the lives of his own self, his wife and his minor son respectively.

Compute the total income of Mr. Ramesh for the current assessment year if his two children are studying in school.

[**Hints:** Value of rent-free house 6,000 × 10/12 = Rs. 5,000, Salary Income Rs. 53,300; House Property income—Nil; Total Income Rs. 53,300; Q.A. for rebate u/s 88 Rs. 20,600] [P-15]

Q. No. 25

A, carrying on the business of manufacturing small tools, receives during the year ending 31st March, 1997 rent from 3 house properties, uses one house property of his own as his factory and office premises and occupies another house

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property of his own for his own residential purposes. The particulars are given below:

(*a*) House property at Calcutta constructed by him on 31st Dec. 1991 on his own land let out to persons for use as their residence. The house consists of 4 flats of equal dimensions, the rent for each flat being Rs. 550 per month. Municipal tax of the entire property is Rs. 5,600 which is paid by A. He paid interest of Rs. 4,000 on a loan taken to construct the house. A is responsible for repair works, but he spent nothing on repairs during the year.

(*b*) House property at Calcutta constructed by him on lease-hold land in 1951 and let out to a tenant at a rent of Rs. 500 per month. Municipal tax Rs. 1,200 is paid by the tenant. Repair expenses of Rs. 600 borne by A. He pays lease rent of Rs. 50 per month.

(*c*) House property at Calcutta taken on rent from B at a rent of Rs. 350 per month. A has sublet it at a rent of Rs. 600 per month. Municipal tax and cost of repairs amounting to Rs. 1,500 and Rs. 1,000 respectively are borne by A.

(*d*) Factory and office premises have got an annual value of Rs. 12,000. The municipal tax and cost of repairs were Rs. 1,000 and Rs. 3,000 respectively.

(*e*) The residential house of A can fetch a rent of Rs. 750 per month. The municipal tax was Rs. 1,500 while the repairs cost amounted to Rs. 1,200.

A's income from all sources other than what has been described above during the year ended 31st March, 1997 amounted to Rs. 40,000.

During the year he purchased National Savings Certificates (VIII issue) for Rs. 10,000. He paid Rs. 500 to income-tax practitioner for income-tax advice.

Compute A's total income for the assessment year 1997-98.

[Calcutta, B.Com.]

[**Hints:** (*a*) Rs. 4,000; (*b*) Rs. 4,200; (*c*) Other sources, Rs. 500; (*d*) NIL; (*e*) NIL; Total Income Rs. 48,700; Q.A. u/s 88 Rs. 10,000] [P-16]

Q. No. 26

Mr. Sen is the owner of four houses in Calcutta, particulars of which are given below:

House No.	I	II	III	IV
Construction started on	1.1.82	1.12.85	1.4.85	1.3.84
Construction completed on	1.1.85	1.5.86	31.12.91	30.6.89
Used for	Own residence	Own business	Tenant's residence	Tenant's business
	Rs.	Rs.	Rs.	Rs.
Rent received during the year	—	—	5,500	5,400
Fair rent	6,000	7,000	5,600	9,000
Municipal value	6,200	6,700	7,000	6,000
Municipal tax—assessed at 10% of valuation			Paid by tenant	600
Cost of repairs	500	300	Nil	Paid by tenant
Collection charges	—	—	360	480
Interest on Loan	—	—	—	300
Vacancy period	2 months	—	1 month	

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Additional Information:

(*i*) Mr. Sen alongwith his family stayed away from Calcutta for 2 months at Delhi on official duty.

(*ii*) Interest was paid on loan obtained by mortgaging the house for the purpose of the marriage of Mr. Sen's daughter.

(*iii*) During the year Mr. Sen won Rs. 12,000 from a lottery.

(*iv*) Mr. Sen's "Salaries" for the previous year amounted to Rs. 31,500.

On the basis of the particulars given above, compute the total income of Mr. Sen for the assessment year 1997-98.

[Calcutta University, B.Com. (Hons.) 1982]

[**Hints:** House I Rs. NIL; House II NIL; House III Rs. 3,082; House IV Rs. 6,720; Salary income Rs. 21,000: Other Sources Rs. 7,000; Total Income Rs. 37,802] [P-17]

Q. No. 27

Calculate the Total Income of Sh. Sham Sunder Samajpati (unmarried) for the assessment year 1997-98 on the basis of the following particulars:

	Rs.
(*a*) Income from House Property (Computed)	42,000
(*b*) One-third share in the Hindu undivided family income of Rs. 1,02,000	34,000
(*c*) Rupee Dividends after deduction of tax @ 20%	48,000
(*d*) Loss from Business	(–)40,000
(*e*) One-fourth share in an association of persons assessed on Business Profits of Rs. 52,000	13,000
(*f*) Loss in share Speculation Business	15,000
(*g*) Interest on Dharamatalla Post Office Saving Bank Account No. 4362	5,500
(*h*) Life Insurance Premium paid in January, 1997 (Capital value with Profits Rs. 50,000)	8,000

[Adopted I.C.W.A.]

[**Hints:** G.T.I. Rs. 75,000; Deduction u/s 80 L Rs. 15,000; Total Income Rs. 60,000 Q.A. for rebate u/s 88 Rs. 8,000; Share in H.U.F. and Interest on P.O.S.B. exempted: speculation loss C/F] [P-33]

Q. No. 28

Mr. X had a Gross Total Income of Rs. 4,00,000 which included Rs. 10,000 as long term capital gains for the assessment year 1997-98. During the year Mr. X made the following donations:

	Rs.
(*a*) National Defence Fund	10,000
(*b*) Prime Minister's National Relief Fund	1,00,000
(*c*) To Family Planning Association of India	10,000
(*d*) All India Congress Committee	1,00,000
(*e*) University of Allahabad (Notified as Institute of National Eminence)	50,000
(*f*) Notified charitable hospital	50,000
	3,20,000

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In addition to the above he paid Life Insurance Premium of Rs. 15,000 on a Policy of Rs. 1,00,000. You are requested to advise your client and compute the relief in respect of Donations and Life Insurance Premium.

[Adapted C. A. Final]

[**Hints**: Q.A. for deduction u/s 80G Rs. 1,99,000; Deduction u/s 80G Rs. 1,79,500. Total Income Rs. 2,20,500; Q.A. for rebate u/s 88 Rs. 15,000] [P-2]

Q. No. 29

Shri Ram Lakhan has prepared the following Profit and Loss A/c for the year ending 31st March, 1997. Compute his total income.

	Rs.		Rs.
To Salaries	15,000	By Gross Profit	85,680
,, Advertisement	5,800	,, Rent of House Property let out	12,000
,, Sundry Expenses	8,500	,, Interest on Government Securities (Gross)	2,400
,, Rent, rates & taxes	950	,, Interest on debentures (net)	2,772
,, Interest on Capital	2,500	,, Winning from Lottery	10,000
,, Fire Insurance premium (Rs. 600 relates to house property)	960		
,, Income-tax	2,875		
,, Household expenses	10,750		
,, Audit fees	1,125		
,, Wealth Tax	3,000		
,, Bad Debts	1,300		
,, Provision for Bad Debts	5,000		
,, Repairs of house property	1,600		
,, Municipal taxes (house property)	2,000		
,, Life Insurance premium	5,500		
,, Donation to National Defence Fund	4,150		
,, Depreciation (allowable)	7,500		
,, Net Profit	34,342		
	1,12,852		1,12,852

The assessee owns one house property (construction started on 1.10.86 and completed on 30.6.91) which is being used by him for the following purposes:

(*i*) 1/4th as his business premises,

(*ii*) 1/4th for residence,

(*iii*) 1/4th has been let out at Rs. 500 p.m. to a tenant who is using it for his residential purposes, and

(*iv*) 1/4th has been let out to a tenant who is using it as his business premises.

[Panjab, B.Com.]

[**Hints:** Business Profit Rs. 44,095 (3/4th of Fire Insurance Premium, Municipal Taxes & repairs of property are only to be disallowed); House Property Rs. 7,630.

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Other sources Rs. 10,865; G.T.I. Rs. 62,590 Deductions u/s 80G Rs. 2,075, 80L Rs. 2,400; Total Income Rs. 58,115 ; Q.A. for rebate u/s 88 Rs. 5,500] [P-19]

Q. N. 30

Given below is the Profit and Loss Account of Shri Rangaswamy for the previous year ending 31st March:

	Rs.		Rs.
To Salaries	25,000	By Gross Profit	1,48,370
,, Printing & Stationery	20,000	,, Discounts	5,000
,, Rates & taxes	10,000	,, Profit on sale of Land (owned since 1961)	10,000
,, Trade Expenses	4,000	,, Dividend (Gross)	1,600
,, Electric Charges	1,500		
,, Extension of shop building	10,000		
,, Carriage	5,000		
,, Provisions: for			
Depreciation	2,000		
Reserve for Bad Debts	8,000		
Reserve for Income-tax	10,000		
Reserve for Sales-tax	10,000		
,, Charities	2,000		
,, Donations (To approved bodies)	2,000		
,, Interest on capital	8,000		
,, Advertisements	5,000		
,, General Expenses	10,000		
,, Net Profit	50,470		
	1,64,970		1,64,970

Compute the total income of Mr. Rangaswamy for the assessment year 1997-98 after taking into account the following:

1. Advertisement including Rs. 2,000—spent on the calendars and diaries.
2. General expenses include Rs. 3,000—spent for promotion of family planning amongst the workers.
3. Actual bad debts amounts to Rs. 4,000.
4. Allowable depreciation (on all assets including additions to building) is Rs. 1,500.
5. The assessee has received demand notice of sales-tax amounting to Rs. 10,000 which he has not disputed.

[**Hints:** Business Income Rs. 88,370: L.T. Capital gain on land—10,000; Dividend Rs. 1,600; G.T.I. Rs. 99,970; Deduction u/s 80L Rs. 1,600, 80G Rs. 1,000; Total Income Rs. 97,370. No deduction of exp. on family planning as it is allowed to companies only. Sales tax liability not allowed] [P-34]

Q. No. 31

The following P & L A/c and the summary of Capital Account are furnished to you by Mr. Amarlal, with a request to compute his taxable income under Income Tax Act.

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Profit and Loss A/c for the year ending 31.3.97

Dr.	Rs.	Cr.	Rs.
To Salaries to Staff	7,200	By Trading Profit	27,000
,, Salary to Amarlal c/d	6,000	,, Commission and damages received from a supplier for wrong goods delivered	5,000
,, Printing & Stationery	750		
,, Rent paid to Amarlal c/d	900		
,, Misc. Exp. of Amarlal	3,000		
,, Int. on Capital c/d	1,150		
,, Insurance Premium	4,600		
,, Commission paid	2,400		
,, Profit for the year c/d	6,000		
	32,000		32,000

Amarlal's Capital Account

	Rs.		Rs.
To Drawings	14,100	By Opening balance	11,500
,, Insurance premium paid on minor son's life	1,400	,, Int. on Capital b/d	1,150
,, House Property Taxes	350	,, Pension from Government	5,200
,, Balance c/f	43,600	,, Provident Fund amounts received on retirement from government service	18,000
		,, Race winnings	3,200
		,, Profit for the year b/d	6,000
		,, Gifts received from father	7,500
		,, Salary b/d	6,000
		,, Rent b/d	900
	59,450		59,450

The following further information is gathered from Mr. Amarlal.

(*a*) He retired from government service at the beginning of the year. He had received a gratuity of Rs. 24,000 which amount he has directly invested in fixed deposit with a nationalised Bank @ 9% p.a. which was received during the year.

(*b*) Insurance premium charged to P & L A/c includes Rs. 600 being premium against loss of profits and the balance L.I.C. premium on Amarlal's life. The sum assured is Rs. 50,000.

(*c*) Amarlal owns a property—half of it is used for business and the other half used for *his residence*.

[C.A. Inter]

[Hints: Salary Income Rs. 3,467 (Standard deduction @ $33^1/_3$% of pension allowed). House Property NIL; Business Profit Rs. 20,875. Other sources Rs. 2,860; G.T.I. Rs. 27,202; Deduction u/s 80L Rs. 2,160. Total Income Rs. 25,042] **[P. 20].**

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Q. No. 32

Calcutta Stores: Trading and Profit and Loss A/c for the year ended 31.3.97.

	Rs.		Rs.
To Opening Stock	5,500	By Sales	37,650
,, Purchases	20,640	,, Closing Stock	7,700
,, Wages	6,700		
,, Gross Profit c/d	12,510		
	45,350		45,350
To Salaries	3,500	By Gross Profit b/d	12,510
,, Rent	800	,, Interest on investment in Securities (Net)	1,600
,, Interest on Capital	400	,, Bad Debts Recovered	700
,, Interest on loan	900	,, Profit on sale of shares (Short-term)	2,000
,, Life Insurance Premium	300	,, Discount	3,000
,, Fire Insurance Premium	120		
,, Bad Debts	800		
,, Provision for Bad Debts	250		
,, Provision for Income-tax	1,500		
,, Depreciation	2,300		
,, Loss on theft	1,000		
,, Entertainment Expenses	4,200		
,, Investment Deposit Account	2,000		
,, Donations	1,000		
,, Net Profit	740		
	19,810		19,810

Additional Information:

(*i*) Both opening and closing stock were valued below cost by 10%.

(*ii*) Sales include Rs. 2,000 being the book value of certain trading goods withdrawn by Mr. Sarkar for his personal use. The cost of the goods was Rs. 2,000 and the market value on the date of withdrawal Rs. 2,500.

(*iii*) Bad debts include Rs. 200 due from a customer against whom a suit for realisation of the debt has been pending for three years in court.

(*iv*) Bad debt recovered was in respect of a claim of Rs. 2,000 in the preceding year out of which a sum of Rs. 1,500 only had been allowed in the year.

(*v*) Depreciation admissible on old and new plant and machinery as per Income Tax rules, Rs. 2,150.

(*vi*) Donation was made to the Government of India for Family Planning.

Compute the total income of Mr. S. Sarkar, a sole proprietor for the assessment year 1997-98.

[Calcutta University, B.Com. (Hons.) 1982]

[Hints: Business Profit—2,685; Bad debt recovered exempted Rs. 500; Taxable Rs. 200; Short Term Capital Gain Rs. 2,000. Income from other sources Rs. 2,000; G.T.I. Rs. 6,685; Deduction 80G Rs. 669. Income Rs. 6,016 Q.A. for rebate u/s 88 Rs. 300] [P-23].

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Q. No. 33

X, a resident, is a practising chartered accountant. He also runs a private accountancy coaching institute. He keeps his accounts on cash basis and his summarised cash account for the year ended 31st March 1997 is as under:

	Rs.		Rs.
To Balance b/d	7,000	By Office expenses	4,000
,, Income from other accounting work	5,400	,, Municipal tax (property)	400
,, Audit fees	14,700	,, Institute expenses	900
,, Institute fees	2,100	,, Personal expenses	3,500
,, Examiner's fees	600	,, Membership and certificate fees	200
,, Withdrawal from PPF	60,000	,, Life insurance premium	7,000
,, Interest on investments (tax deducted at source at the rate of 10%)	9,000	,, Income-tax	2,500
		,, Motor car purchased	75,000
,, Rent from property constructed on 31.1.1992 and let out for residential purposes	5,200	,, Motor car expenses	600
		,, Insurance of property	140
		,, Balance c/d	9,760
	1,04,000		1,04,000

Having regard to the following information, compute his total income for the assessment year 1997-98.

(*a*) One-third of motor car expenses are in respect of his professional practice.

(*b*) Depreciation @ 20% for motor car is Rs. 15,000. *[B.Com., Calcutta]*

[**Hints:** Income from other sources Rs. 10,000; House Property Rs. 1,300; Professional Gain Rs. 12,500; Total Income Rs. 23,800 Q.A. for rebate u/s 88 Rs. 7,000] [P-24].

Q. No. 34

The following is the Profit and Loss Account of Mr. Chenkoti for the year ended on 31st March, 1997.

	Rs.		Rs.
To Salaries & Wages	36,000	By G.P.	1,44,600
,, Trade Expenses	4,350	,, Dividends from a Domestic Co. (Net)	8,000
,, Household Expenses	10,500	,, Rent from Buildings and Godowns let out	15,900
,, Rent and Rates (Rs. 3,600 for property let)	9,600	,, Income from other sources	9,600
,, Postage and Telegrams	825		
,, Life Insurance Premium on the Life of Employees	6,000		
To Donations to N.D.F.	3,000		
,, Discount	3,750		

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,, Audit Fee	2,400	
,, Fire Premium (Rs. 4,800 for property let)	9,000	
,, Loss in Shares (short-term)	6,000	
,, Interest on Capital	600	
,, Income tax	9,900	
,, General Expenses	10,000	
,, Net Profit	66,175	
	1,78,100	1,78,100

Compute his income from business and also the total income for the A.Y. 1997-98.

[**Hints:** House property Rs. 5,040; Business Profits Rs. 71,075; Short-term capital loss Rs. 6,000 to be C/F Other sources Rs. 19,600; Deductions u/s 80L Rs. 10,000, 80G Rs. 1,500; Total income Rs. 84,215] [P-35]

Q. No. 35

Sri Viswanath is practising as a lawyer at Bangalore. He keeps his books on cash basis and his summarised receipts and payments account for the year ended 31.3.1997 is as under:

	Rs.		Rs.
To Balance b/d	2,150	By Subscription for law journals	400
,, Legal charges	1,30,000	,, Law books purchased	1,700
,, Special commission fees	500	,, Rent	1,500
,, Salary as part-time lecturer in Law	24,000	,, Car expenses	2,000
,, Examiner's fees from Mysore University	400	,, Office expenses	5,000
,, Interest on fixed deposits in bank	300	,, Electric charges	1,000
,, Sale proceeds of property	60,950	,, Income-tax	2,000
,, Dividends from a cooperative society	1,000	,, Gifts to daughter	1,000
,, Director's fees	100	,, Household expenses	15,000
,, Maturity amount from ULIP	39,900	,, Donations to approved Institutions	1,000
		,, Car purchased	80,000
		,, Life Insurance premium	5,000
		,, Balance c/d	1,43,700
	2,59,300		2,59,300

The following information is also given:

(*a*) Rent and electric charges are is respect of the premises; one-half of which is used by him as his residence and the remaining half is for office use.

(*b*) One-half of the car expenses are in respect of his personal use.

(*c*) Depreciation on car is to be charged @ 20%.

(*d*) Life insurance premium has been paid on a policy of Rs. 40,000 taken on his own life.

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(*e*) He claimed Rs. 200 for books purchased for his employment purposes and the remaining Rs. 1500 for his professional use. Depreciation on books claimed @ 25%.

(*f*) Fair market value of property on 1.4.81 was Rs. 19,000 and it was acquired in 1980.

[C.I.I. for 1981-82 is 100 and for 96-97 is 305]

You are required to prepare a statement showing his income from profession and also compute his total income for the assessment year 1997-98.

[Mysore, B.Com.]

[**Hints:** Salary Income Rs. 16,000; Professional Gain Rs. 1,13,750; Capital Gain Rs. 3,000; Other source Rs. 1,400; 80G Rs. 500, 80L Rs. 1,300; Total Income Rs. 1,32,350] [Q.A. for rebate u/s 88 Rs. 5,000] [P-36]

Q. No. 36

Mr. Kumar of Bombay submits the following Trading and Profit & Loss A/c for the year ended 31st March 1997. He is also in employment with a cinema company in Bombay. Compute the taxable income for the assessment year 1997-98.

	Rs.		Rs.
To Opening Stock	60,000	By Sale	4,20,000
,, Purchases	3,90,000	,, Closing Stock	80,000
,, Freight	15,000		
,, Gross Profit	35,000		
	5,00,000		5,00,000
To Salaries and Wages	14,800	By Gross Profit	35,000
,, Rent-Taxes	3,800	,, Dividends on shares (Gross)	2,000
,, Household expenses	2,400	,, Rent from Building let out	4,800
,, Income-tax	400		
,, Advance Income-tax	200		
,, Sales Tax	400		
,, Donations	500		
,, Life Insurance Premium	1,800		
,, Audit Fees	200		
,, Reserve for Bad and Doubtful Debts	680		
,, Bad Debts	420		
,, Miscellaneous Expenses	600		
,, Depreciation	500		
,, Net Profit	15,100		
	41,800		41,800

The following information is also supplied by him:

(*i*) He received a salary of Rs. 12,000 from the cinema company in Bombay and has contributed 15% of his salary to a recognised Provident Fund.

(*ii*) Purchases include Rs. 5,000 as advance to his supplier in March, 1997 against goods to be delivered in April, 1997.

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(*iii*) Rent and taxes include Rs. 1,800, being municipal taxes paid for the building let out.

(*iv*) Premium is paid on his life policy of Rs. 15,000.

(*v*) Donation is paid to an approved charitable institution.

(*vi*) Miscellaneous expenses include Rs. 400 being the purchase of books for his employment.

(*vii*) Depreciation permissible is Rs. 400.

[B.Com. (Hons.) Delhi & Mysore University]

[**Hints:** Salary Income Rs. 8.000: House Property Rs. 2,400. Business Profit Rs. 21,580; Other Sources Rs. 2,000. Deduction u/s 80L Rs. 2,000 u/s 80G Rs. 250; Total Income Rs. 31,730; Q.A. for rebate u/s 88 Rs. 3,600] [P-37]

Q. No. 37

Mr. A an individual is a whole-selling agent of a manufacturing company. According to the P & L A/c for the year ending 31-3-97 net profit was Rs. 2,00,000. His P & L A/c includes the following items :

Credit Side :

	Rs.
(*i*) Winning from U.P. State Lottery	25,000
(*ii*) Realisation of a bad debt written off in the year ended 31.3.96. In computing the income of the assessment year. 1994-95 the I.T.O. had allowed this bad debt to the extent of Rs. 15,000 only.	20,000
(*iii*) Refund of Wealth Tax	1,000
(*iv*) Interest received u/s 214 of the I.T. Act for Advance Tax on 2-5-1996	2,000
Debit Side :	
(*v*) Donations to Government to be utilised for family planning	5,000
(*vi*) Wealth Tax for Assessment year 1996-97	1,500
(*vii*) Speculation Loss	5,000

A scrutiny of the statements and accounts showed the following :

(*a*) The assessee purchased a second-hand car of German make on 2-4-1996 for a sum of Rs. 32,000 and claimed depreciation thereon at 25% in the P & L A/c Rs. 8,000.

(*b*) The assessee is a shareholder with substantial interest in a private limited company. The I.T.O. assessing the company has reported that it had given a loan of Rs. 20,000 to the assessee on 1-5-1996 which he repaid on 1-5-1997. The company had accumulated profits of Rs. 50,000 as on 31-3-1996 and Rs. 60,000 as on 31-3-1997.

Compute the Total Income of the assessee for the Assessment Year 1997-98 giving reasons for all additions, deductions, or disallowance. *[I.T.O. Exam.]*

[**Hints :** Business Income Rs. 1,86,500; Other sources – Deemed Dividend Rs. 20,000 + Lottery Rs. 20,000 + Interest Rs. 2,000 GTI Rs. 2,28,500 Deduction u/s 80G Rs. 5,000 and 80L Rs. 15,000; No depreciation on imported car, Loan given by a company to a person who has substantial interest is deemed dividend] [P-18]

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Q. No. 38

Mr. X provides you following information and request you to compute his total income :—

	Rs.
(*a*) Profit from a new industrial unit set up during 1994-95 in small scale sector	80,000
(*b*) Dividend from Indian Co.	15,000
(*c*) Dividend from Foreign Co.	4,000
(*d*) Profits from Poultry Farming business	60,000
(*e*) Rent paid for residential house of Mr. X at Chandigarh—Rs. 30,000 p.a.	
(*f*) His mother is 75 years old and has lost her eyesight.	

How much amount he should invest in N.S.C. VIII issue so that his tax liability is NIL ?

[**Hints :** P & G Rs. 1,40,000; Other sources Rs. 19,000; Deductions u/s 80DD Rs. 15,000; u/s 80IA Rs. 20,000 u/s 80JJ Rs. 20,000 u/s 80L Rs. 15,000 Total income Rs. 89,000. No deduction u/s 80GG at Chandigarh. He can reduce his tax liability to NIL by depositing Rs. 58,500 (11,700 × 100/20) in N.S.C. VIII issue.] [P-38]

QUESTIONS

1. What tax relief is available to an employee in respect of dividend, interest on units of U.T.I. or Mutual funds and interest earned from bank ?

[P.U. and Aligarh University, B.Com. (Hons.)]

2. What are the provisions relating to deductions from Gross Total Income of donations to certain funds, charitable institutions etc. under section 80G of the Income Tax Act, 1961 ?

[Guru Nanak, B.Com.]

3. What do you understand by the Qualifying amount u/s 80G? Who is entitled to it and what are the provisions of the Act in this connection ?

4. Discuss briefly the provisions of the Income Tax Act regarding deductions to be made in computing the total income of an assessee in respect of certain payments.

[Delhi, B.Com. (Hons.)]

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PART III

COMPUTATION OF TAX
(ASSESSMENT YEAR 1997-98)

1. SCHEDULE OF RATES OF TAX
2. TAX FREE INCOMES, INCOMES ENTITLED TO REBATE AND RELIEF
3. DOUBLE TAXATION RELIEF
4. SPECIAL PROVISIONS RELATING TO AVOIDANCE OF TAX
5. COMPUTATION OF TAX LIABILITY

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1 SCHEDULE OF RATES OF TAX

PART—RATES FOR DEDUCTION OF TAX AT SOURCE

[Financial Year 1996-97 (Assessment Year 1997-98)]

In every case in which under the provisions of sections 193, 194, 194A, 194B, 194BB, 194D and 195 of the Income-tax Act, tax is to be deducted at the rates in force, deduction shall be made from the income subject to deduction at the following rates :—

1. In the case of a person other than a company—Rate of Income-tax

(*a*) where the person is resident in India—

(*i*)	on income by way of interest other than "Interest on securities"	10 per cent;
(*ii*)	on income by way of winnings from lotteries and crossword puzzles	40 per cent;
(*iii*)	on income by way of winnings from horse races	40 per cent;
(*iv*)	on income by way of insurance commission	10 per cent;
(*v*)	on income by way of interest payable on—	10 per cent;

(*A*) any security, other than a tax-free security, of the Central or a State Government;

(*B*) any debentures or other securities for money issued by or on behalf of any local authority or a corporation established by a Central, State or Provincial Act;

(*C*) any debentures issued by a company where such debentures are listed on a recognised stock exchange in India in accordance with the Securities Contracts (Regulation) Act, 1956 and any rules made thereunder;

(*vi*)	on any other income	20 per cent;

(*b*) where the person is not resident in India—

(*i*)	in the case of a non-resident Indian—	
	(*A*) on investment income and long-term capital gains	20 per cent;
	(*B*) on income by way of dividends and interest payable by Government or an Indian concern on moneys borrowed or debt incurred by Government or the Indian concern in foreign currency	20 per cent;

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(*C*) on income by way of winnings from lotteries and crossword puzzles — 40 per cent;

(*D*) on income by way of winnings from horse races — 40 per cent;

(*E*) on the whole of other income — income-tax at 30 per cent of the amount of income

or

income-tax in respect of of the income at the rates prescribed in Sub-Paragraph I of Paragraph A of Part III of this Schedule, if such income had been the total income whichever is higher;

(*ii*) in the case of any other person—

(*A*) on income by way of dividends and interest payable by Government or an Indian concern on moneys borrowed or debt incurred by Government or the Indian concern in foreign currency, and income payable in respect of units (not being income payable to an individual) purchased in foreign currency, of the Unit Trust of India — 20 per cent;

(*B*) on income by way of winnings from lotteries and crossword puzzles — 40 per cent;

(*C*) on income by way of winnings from horse races — 40 per cent;

(*D*) on income by way of long-term capital gains, — 20 per cent;

(*E*) on the whole of other income — income-tax at 30 per cent of the amount of income

or

income-tax in respect of the income at the rates prescribed in Sub-Paragraph I of Paragraph A of Part III of this Schedule, if such income had been the total income, whichever is higher.

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2. In the case of a company—

(*a*) Where the company is a domestic company—

(*i*)	on income by way of interest other than "Interest on securities"	20 per cent;
(*ii*)	on income by way of winnings from lotteries and crossword puzzles	40 per cent;
(*iii*)	on income by way of winnings from horse races	40 per cent;
(*iv*)	on any other income	21.5 per cent

(*b*) Where the company is not a domestic company—

(*i*)	on income by way of dividends payable by any domestic company	20 per cent;
(*ii*)	on income by way of winnings from lotteries and crossword puzzles	40 per cent;
(*iii*)	on income by way of winnings from horse races	40 per cent;
(*iv*)	on income by way of interest payable by Government or an Indian concern on moneys borrowed or debt incurred by Government or the Indian concern in foreign currency	20 per cent;
(*v*)	on income by way of royalty payable by Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after the 31st day of March, 1976, where such royalty is in consideration for the transfer of all or any rights (including the granting of a licence) in respect of copyright in any book on a subject referred to in the first proviso to sub-section (1A) of section 115A of the Income-tax Act, to the Indian concern, or in respect of any computer software referred to in the second proviso to sub-section (1A) of section 115A of the Income-tax Act, to a person resident in India.	30 per cent;
(*vi*)	on income by way of royalty [not being royalty of the nature referred to in sub-item (*b*)(*v*)] payable by Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern and where such agreement is with an Indian concern, the agreement is approved by the Central Government or where it relates to a matter included in the industrial policy,	

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for the time being in force, of the Government of India, the agreement is in accordance with that policy—

(*A*) where the agreement is made after the 31st day of March, 1961 but before the 1st day of April, 1976 — 50 per cent;

(*B*) where the agreement is made after the 31st day of March, 1976 — 30 per cent;

(*vii*) on income by way of fees for technical services payable by Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern and where such agreement is with an Indian concern, the agreement is approved by the Central Government or where it relates to a matter included in the industrial policy, for the time being in force, of the Government of India, the agreement is in accordance with that policy—

(*A*) where the agreement is made after the 29th day of February, 1964 but before the 1st day of April, 1976 — 50 per cent;

(*B*) where the agreement is made after the 31st day of March, 1976 — 30 per cent;

(*viii*) on income by way of long-term capital gains — 20 per cent;

(*ix*) on any other income — 55 per cent

Explanation—For the purposes of item 1(*b*) (*i*) of this Part, "investment income" and "non-resident Indian" shall have the meanings assigned to them in Chapter XII-A of the Income-tax Act.

Surcharge on income-tax

The amount of income-tax deducted in accordance with the provisions of subitem (*a*) of item 2 of this Part (*i.e.* in case of domestic company only) shall be increased by a surcharge, calculated at the rate of fifteen per cent of such income-tax.

PART II—RATES OF INCOME-TAX FOR ASSESSMENT YEAR 1997-98

1. In the case of every individual or Hindu undivided family or association of persons or body of individuals, whether incorporated or not, or every artificial juridical person,

(1) where the total income does not exceed Rs. 40,000 — *Nil*;

(2) where the total income exceeds Rs. 40,000 but does not exceed Rs. 60,000 — 15 per cent of the amount by which the total income exceeds Rs. 40,000;

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(3) where the total income exceeds Rs. 60,000 but does not exceed Rs. 1,20,000	Rs. 3,000 *plus* 30 per cent of the amount by which the total income exceeds Rs. 60,000;
(4) where the total income exceeds Rs. 1,20,000	Rs. 21,000 *plus* 40 per cent of the amount by which the total income exceeds Rs. 1,20,000.

2. In the case of every co-operative society,—

(1) where the total income does not exceed Rs. 10,000	10 per cent of the total income;
(2) where the total income exceeds Rs. 10,000 but does not exceed Rs. 20,000	Rs. 1,000 *plus* 20 per cent of the amount by which the total income exceeds Rs. 10,000;
(3) where the total income exceeds Rs. 20,000	Rs. 3,000 *plus* 35 per cent of the amount by which the total income exceeds Rs. 20,000.

Paragraph C

3. In the case of every firm, assessed as firm

On the whole of the total income — 40 per cent

4. In the case of every local authority—

On the whole of the total income — 30 per cent

5. In the case of a company—

I. In the case of a domestic company — 40 per cent of the total income ;

II. In the case of a company other than a domestic company—

(*i*) on so much of the total income as consists of—

(*a*) royalties received from Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after the 31st day of March, 1961 but before the 1st day of April, 1976, or

(*b*) fees for rendering technical services received from Government or an Indian concern in pursuance of an agreement made by it with be Government or the Indian concern after the 29th day of February, 1964 but before the 1st day of April, 1976, and where such agreement has been approved by the Central Government. — 50 per cent

(*ii*) On the balance, if any, of the total income — 55 per cent

Surcharge—@ $7^1/_2$% of tax in case of domestic companies only whose total income exceeds Rs. 75,000.

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PART III—RATES OF TAX FOR ASSESSMENT YEAR 1997-98 (SPECIAL INCOMES]

1. Long term capital gains [Section 112]

(*a*) *If assessee has only long term capital gain and no other income during the year:—*

An amount equal to exempted limit shall be deducted out of long term capital gain and on balance amount tax will be levied at the rate of 20%. In case of partnership firm assessed as firm (PFAF) the rate of tax is 20% with no exempted limit.

(*b*) *If assessee has long term capital gain and other income as well :—*

(*i*) Tax will be calculated at scheduled rates on total income after it has been reduced by the amount of long term capital gain, if any.

(*ii*) On long term capital gain tax will be calculated at the rate of 20% [for PFAF 20%]

(*iii*) In case the total income after being reduced by long term capital gain is less than exempted limit, the amount of capital gain will be reduced by the amount of shortfall between exempted limit and other total income.

(*c*) *Deduction u/s 88.* For allowing deductions u/s 80 gross total income shall be reduced by the amount of long term capital gain, if included. The balance amount will be deemed as G.T.I.

(*d*) *Rebate u/s 88.* Rebate u/s 80 shall not be allowed out of tax on long term capital gain. It shall be restricted to tax on total income as reduced by long term capital gain.

2. In case of block assessment u/s 115ABC. The rate of tax is 60% [Section 113]

3. In case of winnings from lotteries, puzzles, races, card games, gambling and betting [Section 115BB]

(*a*) Income by way of winnings from lotteries, crossword puzzles, card games, gambling and betting—40%

(*b*) Balance Total income—Scheduled rates.

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2 TAX FREE INCOMES AND INCOMES ENTITLED TO REBATE AND RELIEF

Rebateable Incomes—Share from A.O.P.—Average rate—Rebate on savings u/s 88—Rebate on Investment u/s 88A—Relief u/s 89 (1) —Relief u/s (2)—Questions.

In the previous chapter those incomes were discussed which are altogether exempted from tax. These incomes are not added in the Gross Total Income of an assessee either fully or partially. But there are certain incomes which are fully added in the Gross Total Income of assessee for the purposes of calculation of tax. These incomes can be grouped under three categories.

I. Tax Free Incomes forming part of total income but entitled to rebate of tax (Section 86).

II. Savings and Investments entitled to Rebate of tax (Section 88 and 88A).

III. Incomes included in total income but entitled to relief of tax [Sections 89(1)(a) and 89(2)].

I. TAX FREE INCOMES [Rebateable Incomes]

These incomes form part of total income and out of final tax liability a rebate of tax shall be allowed.

REBATE OF TAX u/s 86

1. In case total income of PFAOP/AOP is not taxable at MMR or any other rate higher than MMR—the share of income of a member of PFAOP/AOP shall be added in his total income and shall be eligible for rebate of tax at average rate on such share.

2. In case total income of PFAOP/AOP is taxable at MMR or a higher rate the share of income of a member from such PFAOP/AOP shall not be included in the total income of such member.

3. In case total income of PFAOP/AOP is not taxable at all—the share of income of a member from such PFAOP/AOP shall be fully added in the individual income of such member and is fully taxable. No rebate of tax in this case.

Calculation of rebate

Where there is included in the total income of an assessee, any income on which no income-tax is payable under the provisions of this Act, the assessee shall

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be entitled to a deduction from the amount of income-tax with which he is chargeable on his total income, of an amount equal to the income-tax calculated at the average rate of income-tax on the amount on which no income-tax is payable. (Section 110).

The above section provides that in case any share of income from an association of persons (provided such association is liable to tax) is included in the total income of an assessee, such person shall be entitled to claim a rebate of tax at average rate.

$$\text{Average rate} = \frac{\text{Total Tax}}{\text{Total Income}} \times 100$$

Illustration 1. (*a*) Mr. A has business profit of Rs. 75,000 and received Rs. 8,000 as 1/8th share of profits of an association of persons during the previous year ending on March 31, 1997. Calculate his tax liability.

(*b*) What difference it will make if total income of A is Rs. 37,000 and his 1/8th share from PFAOP (which has no such member whose individual income exceeds Rs. 40,000) is Rs. 28,000 ?

Solution

(*a*) *Computation of Total Income*

		Rs.
Business Profit		75,000
Share of profit from an association of persons—not to be included in total income as PFAOP's income is taxable at MMR.		Nil
	Total Income	75,000

Computation of Tax Liability

First Rs. 40,000 of Total Income	Nil	Nil
Next Rs. 20,000 of Total Income	15%	3,000
Next Rs. 15,000 of Total Income	30%	4,500
	Total Tax	7,500

No rebate u/s 86 as PFAOP has one member (Mr. A) whose total income exceeds the exempted limit.

(*b*) Total Income [Rs. 37,000 + 28,000] 65,000

Tax on Rs. 60,000	3,000	
on Rs. 5,000	1,500	
	4,500	
Less rebate of tax u/s 86 $\frac{4,500 \times 28,000}{65,000}$	1,938	
Net Tax	2,562	

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Q. No. 1

Mr. Rahim is carrying on his own profession as a lawyer and for the assessment year 1997-98 he submits the following particulars :—

(*i*)	Professional Gain	Rs. 108,400
(*ii*)	Share of income from PF AOP (1/4th)	Rs. 16,000
(*iii*)	Share of income from another PF AOP (1/2)	Rs. 16,000

Compute his tax liability for the assessment year 1997-98.

[**Hints :** Tax Rs. 22.760 : No rebate of tax u/s 86 as PFAOP has one member (Mr. Rahim) whose total income exceeds Rs. 40,000 and 1/4th share from PFAOP is not to be added in total income as PFAOP's income is taxable at MMR]

II. SAVING AND INVESTMENTS ENTITLED TO REBATE OF TAX

With effect from assessment year 1991-92 deductions u/s 80C and u/s 80CC have been replaced by Rebate of Tax u/s 88 and 88A. These rebates are:

1. Rebate of tax for savings made in approved schemes [Section 88].
2. Rebate of tax in case of old individuals [Section 88B].

The schemes provide for reduction in tax liability and not the total income.

1. Rebate of Tax on Approved Savings [Section 88]

Out of final tax liability computed on total income, a rebate of tax is allowed.

(*i*) **Rate of Rebate.** Rebate shall be allowed @ 20% of eligible savings subject to a maximum of Rs. 12,000 in a previous year.

In case an individual has made investment as per point(s) below he can claim an additional rebate upto Rs. 2,000 *i.e.* limit of Rs. 12,000 will be raised to Rs. 14,000.

For actors, singers, authors, play writers, sports persons and artists the rate of rebate is 25% of qualifying amount subject to maximum of Rs. 17,500 provided the professional income is 25% or more of total income.

Restriction on Rebate [Section 112 (3)]

In case total income of a person includes long term capital gain the rebate of tax u/s 88 will be allowed only out of income tax on total income as reduced by such long term capital gain.

(*ii*) **Eligible Persons.** This rebate shall be admissible to:

(*a*) Individuals,

(*b*) Hindu Undivided Families,

(*c*) Association of persons or body of individuals consisting only of husband and wife as governed by community of property in force in state of Goa an Union Territories of Daman & Diu.

(*iii*) **Eligible Savings.** Following savings are eligible for rebate of tax provided these are made out of taxable income of the assessee:

(*a*) *Life Insurance Premia.* Any amount paid by assessee as life insurance premium to keep in force an insurance on the life of individual, spouse, or any child of such individual and in case of H.U.F. or A.O.P.—on the life of any member of such H.U.F. or A.O.P. From the assessment year 1996-97 actual premium paid shall fully qualify.

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(*b*) *Any premium paid* to keep in force a contract for deferred annuity (not being an annuity referred to u/s 80 CCA, *i.e.*, Jeevan Dhara policy etc.) on the life of any of the persons mentioned in (*a*) above. Such contract must not contain any provision by which insured person can take cash payment in lieu of annuity.

(*c*) *Any amount deducted* out of salary of an employee by or on behalf of the Government for the purpose of securing to him a deferred annuity—actual amount so deducted or 20% (*i.e.*, 1/5th) of salary whichever is less shall qualify for rebate.

(*d*) *Contribution to Statutory Provident Fund*—any amount contributed by employee towards his provident fund which is governed by Provident Fund Act 1925. Such amount shall fully qualify.

(*e*) *Contribution to P.P.F.*—any amount deposited by employee/assessee in Public Provident Fund (P.P.F.) account on his own name or on the name of spouse or on the name of minor of whom he is guardian shall fully qualify.

(*f*) *Employee's contribution to R.P.F.*—Fully qualifies.

(*g*) *Employee's contribution to approved super annuation fund*—Fully qualifies.

(*h*) *Any Contribution to C.T.D. Account.* In case any amount is deposited by assessee in Post Office 10 yr. or 15 yr. cumulative Time Deposit account on the name of self or any minor child of whom he is guardian shall fully qualify.

(*i*) *Any subscription to Notified security or any deposit scheme* —Any amount invested by assessee in a security which is notified by Central Govt. for this purpose shall fully qualify. Govt. has notified National Saving Scheme 1992 under this sub clause.

(*j*) *Amount invested in national savings certificates VIII issue*—shall fully qualify. Accrued interest will also qualify for rebate.

(*k*) *Amount invested in any other Savings certificates*—shall also qualify fully if such savings certificates are notified by the Central Govt.

(*l*) *Amount invested in Unit Linked Insurance Plan (ULIP) of* Unit Trust of India or of Mutual Fund set up by Life Insurance Corporation on own name or on the name of spouse shall also fully qualify.

(*m*) Any amount paid to keep in force a contract of policy under *Jeevan Dhara* or *Jeevan Akshay* plan of Life Insurance Corporation shall fully qualify.

(*n*) Any amount invested in any units of U.T.I. or other Mutual Funds under any plan approved and notified by the Govt.—actual amount invested or Rs. 10,000 p.a. whichever is less to qualify.

(*o*) Any amount deposited in pension fund to be set up by Mutual Funds or U.T.I. and to be so notify shall fully qualify.

(*p*) *Amount subscribed in deposit scheme of National Housing Bank*—If such deposit scheme is notified by the Central Govt. the amount deposited under such scheme shall fully qualify.

(*q*) *Subscription to Home deposit account.* Any amount subscribed to a deposit scheme of

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(*i*) a public sector company which is engaged in providing long term finance for construction or purchase of houses in India for residential purposes; or

(*ii*) any authority set up in India for providing housing accommodation or improvement of cities, towns and villages shall qualify for rebate u/s 88. Under this section only those deposits shall qualify whose interest is not eligible for deduction u/s 80L and scheme is notified by government.

(*r*) *Amount repaid against House Building Loan or instalment of price paid for house purchased*—Any amount paid for the purposes of purchase or construction of a residential house property, the income from which is chargeable to tax under the head "Income from house property" (or which would, if it had not been used for the assessee's own residence, have been chargeable to tax under that head), where such payments are made toward or by way of—

(*i*) any instalment or part payment of the amount due under any self-financing or other scheme of any development authority, housing board or other authority engaged in the construction and sale of house property on ownership basis; or

(*ii*) any instalment or part payment of the amount due to any company or co-operative society of which the assessee is a shareholder or member towards the cost of the house property allotted to him; or

(*iii*) repayment of the amount borrowed by the assessee from—

1. the Central Government or any State Government, or
2. any bank, including a co-operative bank, or
3. the Life Insurance Corporation, or
4. the National Housing Bank, or
5. any public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase or houses in India for residential purposes which is approved for the purposes of clause (*viii*) of subsection (1) of section 36, or
6. any company in which the public are substantially interested or any co-operative society, where such company or co-operative society is engaged in the business of financing the construction of houses, or
7. the assessee's employer where such employer is a public company or a public sector company or a university established by law or a college affiliated to such university or a college affiliated to such university or a local authority.

(*iv*) stamp duty, registration fee and other expenses for the purpose of transfer of such house property to the assessee.

but shall not include any payment towards or by way of—

(A) the admission fee, cost of share and initial deposit which a shareholder of a company or a member of a co-operative society has to pay for becoming such shareholder or member, or

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(B) the cost of the land, except where the consideration for the purchase of the house property is a composite amount and the cost of the land alone cannot be separately ascertained; or

(C) the cost of any addition or alteration to, or renovation or repair of, the house property which is carried out after the issue of the completion certificate in respect of the house property by the authority competent to issue such certificate or after the house property or any part thereof has either been occupied by the assessee or any other person on his behalf or been let out; or

(D) any expenditure in respect of which deduction is allowable under provisions of section 24.

Actual amount of loan repaid or amount of installments paid or Rs. 10,000 p.a., we is less shall qualify for rebate u/s 88.

(s) With effect from assessment year 1997-98, any investment made in notified units of UTI or Mutual Funds or in notified debentures or shares of certain notified companies shall also qualify for this rebate upto actual amount invested or Rs. 10,000 p.a. whichever is less. No money can be raised against these assets by way of sale or raising loan etc. for 3 years. The assets on which rebate u/s 88 has been claimed shall not qualify for exemption of capital gain u/s 54EA or 54EB.

(*iv*) **Effect of Breach of conditions** [88(7)]

(*a*) Non-payment of Life Insurance premia resulting into termination of contract of insurance for at least two years or termination of contract of insurance by notice shall be treated as breach of condition.

(*b*) Non-payment of contribution to Unit Linked Insurance Plan of L.I.C. or U.T.I. resulting into termination of contract before expiry of five years or termination of contract before expiry of five years or termination of contract by notice shall be treated as breach of condition.

(*c*) The house, in respect of which rebate has been claimed under this section, is transferred before the expiry of 5 years from the date of taking over the possession or any amount is received back as refund or otherwise, shall also lead to breach of condition.

In all these above mentioned cases the effects will be

(*i*) no deduction shall be allowed to the assessee in respect of life insurance premia, or contribution to U.L.I.P. or amount paid under House building loan scheme or purchase or house during the previous year in which such breach takes place; and

(*ii*) the rebate of tax claimed on these savings in preceding previous years shall be disallowed and amount of such rebate shall be added to the tax on total income of the assessee relevant to the assessment year.

Illustration 2. Mrs. Rama jain is working in a office. Her gross salary for the year 1996-97 was Rs. 74,650 having no other income. She has deposited :—

(*i*) Rs. 3,000 in Recognised Provident Fund;

(*ii*) Rs. 6,000 in Public Provident Fund;

(*iii*) Rs. 2,500 under Unit Linked Insurance Scheme UTI;

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(*iv*) Rs. 5,000 in NSC VIII issue.

(*v*) Rs. 2,480 accrued as interest on NSC VIII issue purchased in 1994-95. Compute her tax liability for the year 1997-98.

Solution : *Computation of tax liability*

	Rs.	Rs.
Salary		
Salary received	74,650	
Standard Deduction (maximum)	18,000	
(as her total income before allowing this deduction does not exceed Rs. 75,000 [74,650 + 2,480 – 80L Rs. 2,480]		56,650
Other Sources		
Interest accrued on NSC VIII issue		2,480
G.T.I.		59,130
Deduction u/s 80L		2,480
Total Income		56,650
Tax on Rs. 56,650		
On First Rs. 40,000	NIL	NIL
On Balance Rs. 16,650	15%	2,498
		2,498

Rebate u/s 88

		Rs.
Q.A. (*i*)	Own contribution to RPF	3,000
(*ii*)	Amount deposited under PPF	6,000
(*iii*)	U.L.I.P.	2,500
(*iv*)	Interest Accrued on NSC	2,480
(*v*)	NSC VIII issue purchased	5,000
	Q.A.	18,980

Rebate @ 20% of 18,980 = 3,796 or actual tax whichever is less	2,498
Tax Payable	NIL

Q. No. 2

From the particulars given below compute the tax liability of Mr. Jagjit Singh an artist for the assessment year 1997-98:—

	Rs.
(*a*) Professional Gain	1,00,000
(*b*) L.T.C. Gain	10,000
(*c*) Amount deposited in PPF	50,000
(*d*) Life Insurance Premium	16,000

[**Hints :** Tax (*i*) on LTCG 20% of Rs. 10,000 = Rs. 2,000 + (*ii*) On Balance Total income Rs. 15,000 = Rs. 17,000; Less rebate of tax u/s 88 @ 25% of Rs. 66,000 = Rs. 16,500 but restricted to tax on total income as reduced by LTCG *i.e.* Rs. 15,000. Net Tax Rs. 2,000]

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2. Rebate of Income-tax for old persons [Section 88B]

The Finance Act 1992 has introduced rebate of tax with effect from assessment year 1993-94.

For

(*i*) Individuals;

(*ii*) who are of the age of 65 or above; and

(*iii*) whose gross total income (computed income from all heads but without allowing deduction u/s 80) does not exceed Rs. 1,20,000.

This rebate will be allowed @ 40% of tax on total income. This rebate is to be allowed before allowing any rebate of tax u/s 86, 88, or 89 (1).

Illustration 3. Dr. V.P. Sharma whose age is 69 years has given following details of his income. Compute his tax liability for the assessment year 1997-98 :

(*i*) Pension from Govt. Rs. 54,080

(*ii*) Long Term Capital Gain Rs. 16,250

(*iii*) Interest on units of UTI, Mutual Funds and Fixed deposit with Bank 25,350

(*iv*) Deposited Rs. 10,000 in MEP (an Equity Linked Saving Scheme) and Rs. 10,000 in NSS 1992.

Solution : *Computation of total income*	Rs.	Rs.
I. *Salary* : Pension	54,080	
Standard Deduction	18,000	36,080
II. *Capital Gain* : L.T.C. Gain		16,250
III. *Others Sources* : Bank Interest etc.		25,350
Gross Total Income		77,680
Deduction u/s 80 L (Maximum)		15,000
Total Income		62,680

Computation of tax liability

(*i*) Tax on L.T. Capital Gain (16,250 @ 20%)	3,250
(*ii*) Tax on Balance total income at scheduled rate *i.e.* on Rs. 46,430 Rs. 40,000 – Nil — Nil Rest 6,430—15%	965
Total Tax	4,215
(*i*) *Rebate of Tax u/s 88 B ; 40% of Rs. 4,215* = 1,686	

(*ii*) *Rebate of Tax u/s 88*

	Rs.
Investment in MEP	10,000
Amount deposited in NSS	10,000
	20,000

Rebate @ 20% of Rs. 20,000 = 4,000
but restricted to tax on regular income = 965 2,651

Tax Payable 1,564

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Q. No. 3

Mr. Jagdish Singh was born on 1-1-1931. He submits following particulars of his income and asks you to compute his tax liability for the assessment year 1997-98 :—

	Rs.
(*i*) Income including Bank Interest of Rs. 9,600	1,04,000
(*ii*) Amount deposited in NSS 1992	10,000
(*iii*) Winnings from lotteries—not included at (*i*) above.	10,000

[**Hints :** Total Income Rs. 99,400; Tax Rs. 15,320 Rebate u/s 88 Rs. 2,000 u/s 88B Rs. 6,128, Net tax payable Rs. 7,192]

III. INCOMES ENTITLED TO RELIEF

Where, by reason of any portion of an assessee's salary is being paid in arrears or in advance or by reasons of his having received in any financial year salary of more than twelve months or a payment which under provisions of clause (3) of section 17 is a profit in lieu of salary, his income is assessed, at a rate higher than that at which it would otherwise have been assessed, the Assessing Officer, shall on an application made to him in this behalf, grant such relief as may be prescribed. [Section 89(1)].

Where, by reason of any portion of income from interest on securities being received in arrears, an assessee's total income is assessed at a rate higher than that at which it would otherwise have been assessed, the Assessing Officer shall on an application made to him in this behalf grant such relief as may be prescribed. [Section 89(2)].

Relief when Salary is paid in arrears or in advance [Section 89(1)]

Salary or interest on securities are taxable in the previous year in which they are due or received. But in case, following incomes are included in the total income of an assessee, he may apply to the Assessing Officer for relief:

(*i*) Salary being received in arrears or in advance;

(*ii*) Where the payment, in the nature of gratuity in respect of past services extending over a period of not less than 5 years is received;

(*iii*) Where the payment is in the nature of compensation received by an employee from his employer or former employer at or in connection with the termination of employment of the continuous service of not less than three years and where the unexpired portion of the term of employment is also not less than 3 years;

(*iv*) Where the payment is in the nature of commutation of pension;

(*v*) Any other payment, if not covered under (*i*) to (*iv*) above.

All these incomes pertain to the head *Salaries*, and in the first four cases, *i.e.*, (*i*) to (*iv*) relief is to be calculated by the Income-tax Officer and in case (*v*) by the Central Board of Direct Taxes. Relief is to be worked out in accordance with mode prescribed in Rule 21A(2).

Computation of Relief

(a) In case of salary received in arrears or in advance

(*i*) Add the arrears of salary or advance salary in current previous year's income and compute tax on total income so computed.

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(*ii*) Exclude the amount of arrears from the current previous year's income and compute the tax on total income so computed. Calculate the difference between tax at (*i*) and computed tax at (*ii*).

(*iii*) In case arrears of salary or advance salary relate to one previous year—such amount is added in the total income of the previous year to which such arrears belong. On this revised total income tax is calculated.

(*iv*) Calculate the difference between the tax paid in that year and tax payable on revised total income of that previous year.

(*v*) Compare the difference of taxes calculated in point (*ii*) to be called (A) with the difference of taxes calculated in point (*iv*) to be called (B). If tax at (A) is more than tax at (B), the excess will be the amount of relief to be allowed to such assessee.

Illustration 4

	Rs.
Total Income of previous year 1996-97 (without arrears)	42,000
Arrears of salary belonging to previous year 1995-96 but received during 96-97	5,000
Total Income of previous year 1995-96	36,000

Calculate the amount of relief assessee is entitled to in this case.

Solution

Previous year 1996-97/Assessment year 1997-98

		Rs.	Rs.
Step (1):	Current Total Income	42,000	
	Add: Arrears of salary	5,000	
	Total Income	47,000	
	Tax on this total		
	First 40,000	Nil	Nil
	Next 7,000	15%	1,050
	Tax		1,050
Step (2):	Current Total Income	42,000	
	Tax on this total		
	Tax on Rs. 40,000	Nil	
	Tax on Rs. 2,000 15%	300	
	Tax		300
	Net difference		750

Step (3): Calculate the difference between tax at (1) and tax at (2) *i.e.* Rs. 750 to be called figure (A).

Previous year 1995-96—Assessment year 1996-97

Step (4):	Current Total Income	36,000
	Add: Arrears	5,000
	Total Income	41,000

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	Tax on this total		
	First 40,000	Nil	Nil
	Next 1,000	20%	200
	Tax		200
Step (5):	Calculate tax on current total income *i.e.*	36,000	
	Upto Rs. 36,000	Nil	Nil
	Net Difference		200

Step (6): Calculate difference between tax at step (4) and tax at step (5) *i.e.* Rs. 200 to be called figure (B).

Step (7): The difference between tax at figure (A), Rs. 750, and tax at figure (B), Rs. 200, i.e., Rs. 550 is the amount of relief for which assessee is entitled to during the assessment year 1997-98.

Q. No. 4

	Rs.
Total income of the year 1996-97	64,000
Arrears of salary for the year 1995-96 received in 1996-97	3,000
Total income of the previous year 1995-96	37,000

Compute the amount of relief u/s 89(1).

[**Hints :** Relief u/s 89(1) Rs. 900]

(*vi*) In case arrears belong to more than one previous year—the arrears should be got ascertained to different previous years and Step (5) and Step (6) of illustration 2 above to be calculated for each of these previous years and differences in each of these previous years are to be aggregated. Aggregate of these differences will be called figure (B) and rest of the procedure is same to calculate the amount of relief.

(*vii*) Different methods are provided for calculation of relief in cash any gratuity or compensation on termination of employment is included in the total income of the assessee.

(*b*) *When interest on securities is received in arrears (Rule 21B)*

In case, any arrears of interest on securities, which were not taxed on due basis in earlier previous year, are included in the total income of an assessee, the assessee may apply of relief tax to the Assess in Officer.

Method of calculating rebate is same as in illustration 2 (above). Only the words "Arrears of interest on securities" are to be substituted for words "Arrears of Salary." Rest of the method is same.

Q. No. 5

Calculate the amount of rebate of tax u/s 86 and final tax liability of the assessee in following case for the assessment year 1997-98 :—

	Rs.
(*i*) 1/4th share from PFAOP	15,000

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(*ii*) Interest on Govt. Securities 17,000
(*iii*) Other Incomes 59,000

[**Hints :** GTI Rs. 76,000 Deduction u/s 80L Rs. 12,000 Tax on total income Rs. 4,200 Share from PFAOP is not to be added]

Q. No. 6

(*a*) Mr. D is a writer as well as a professional. His income particulars are :—

	Rs.
(*i*) Royalty on Books	42,000
Expenses on writing these books	8,000
(*ii*) Professional income	1,30,000
(*iii*) He deposits Rs. 64,000 in P.P.F.	

Compute his tax liability for assessment year 1997-98.

(*b*) What difference it would make if in above case his royalty is Rs. 52,000 and professional gain is Rs. 1,20,000. Expenses and savings remaining same.

[**Hints :** (*a*) Tax on Rs. 1,64,000 = Rs. 38,600 less rebate of tax Rs. 12,000. (*b*) Tax on Rs. 1,64,000 Rs. 38,600 less rebate of tax @ 25% of 64,000 = Rs. 16,000]

Q. No. 7

During 1996-97 Mr. Prakash received arrears of Rs. 6,000 relating to previous year 1995-96. His total income excluding arrears in 1995-96 Rs. 54,000 and 1996-97 Rs. 64,000.

Compute the amount of relief u/s 89(1).

[**Hints :** Relief u/s 89(1) Rs. 900]

Q. No. 8

Mr. X has the following incomes for the previous year ending 31st March 1997 :—

	Rs.
(*a*) Income from business	20,000
(*b*) Income from commission from agency of an Indian company	15,000
(*c*) Compensation received for the termination of selling agency	75,000
(*d*) He deposited Rs. 40,000 in N.S.S. 1992 on 30.3.97.	

Find out the tax liability for the Assessment year 1997-98.

[Algappa University MCS Degree August, 1995]

[**Hints :** Total Income Rs. 1,10,000 Tax Rs. 18,000 rebate of tax u/s 88 Rs. 8,000]

QUESTIONS

1. Describe the savings which are entitled to rebate of tax u/s 88 ?
2. Define and Distinguish tax free (Rebateable) and exempted incomes. Illustrate your answer.
3. Explain the following with illustration :—
   (*a*) Rebate of tax u/s 86
   (*b*) Relief on arrears of salary u/s 89(1)
   (*c*) Rebate for old aged persons u/s 88B.

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3 DOUBLE TAXATION RELIEF

DOUBLE TAXATION RELIEF

Agreement with Foreign Countries for Avoidance or Relief against Double Taxation (Section 90)

Section 90 of the Income-tax Act, 1961, empowers the Central Government to enter into agreements with the Government of any country for the grant of relief against double taxation or for the avoidance of double taxation. This section also empowers the Central Government to make such provisions as may be necessary for the implementation of such agreement and such provisions may be published in the Official Gazette. Under this section, the Central Government may enter into agreement with foreign countries—

(*a*) for the granting of relief in respect of income on which have been paid both income-tax under this Act and income-tax in that country, or

(*b*) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country, or

(*c*) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country, or investigation of cases of such evasion or avoidance, or

(*d*) for recovery of income-tax under this Act and under the corresponding law in force in that country.

The Central Government has so far entered into agreements for relief against or avoidance of double taxation with many countries and these agreements are in operation.

These agreements may be classified into two parts—

(*a*) Agreement for relief from Double taxation;

(*b*) Agreement for avoidance of Double taxation.

Agreement for Relief from Double Taxation

Under this category assessments provide for the payment of tax in both the countries under the respective laws of those countries but later on rebate of tax is given in both the countries on doubly assessed income. In such case assessee must show that the identical income has been doubly taxed and that he has paid tax both in India and in the foreign country on the same income. *(C.I.T. vs. New Citizen Bank of India Ltd. 58. I.T.R. 468).*

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Agreements for Avoidance of Double Taxation

Under these agreements the assessee has first to pay the tax and then apply for relief in the form of a refund. Each country recovers tax only on that portion of income which accrued within that country and takes into account the income accruing in other country only for rate purposes. In such cases no refund arises.

Countries with which no Agreement Exists

Section 91 provides :

1. If any person who is resident of India in any previous year proves that in respect of his income which accrued or arose during the previous year outside India (and which is not deemed to accrue or arise in India), he has paid, in any country with which there is no agreement under Section 90 for relief or avoidance of double taxation, income-tax by deduction or otherwise, under the law in force in that country he shall be entitled to the deduction from Indian Income-tax payable by him of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of the tax of the said country whichever is the lower; or at the Indian rate of tax, if both are equal.

2. If any person who is resident of India in any previous year proves that in respect of his income, which accrued or arose to him during that previous year in Pakistan, he has paid in that country, by deduction or otherwise tax payable to the Govt. under any law for the time being in force in that country relating to taxation of agricultural income he shall be entitled to a deduction from the Indian income-tax payable by him:

(*a*) of the amount of the tax paid in Pakistan under any law, aforesaid, on such income which is liable to tax under this Act also; or

(*b*) of a sum calculated on that income at the Indian rate of tax, whichever is less.

3. If any non-resident is assessed on his share in the income of a registered firm assessed as resident of India in any previous year and such share includes any income accruing or arising outside India during that previous year (and which is not deemed to accrue or arise in India) in a country with which there is no agreement under Section 90 for the relief or avoidance of double taxation and he proves that he has paid income-tax by deduction or otherwise included, he shall be entitled to a deduction from the Indian income tax payable by him of a sum calculated on such doubly taxed income so included, at the Indian rate of tax or the rate of tax of the said country whichever is lower, or at the Indian rate of tax, if both the rates are equal.

This section provides for—

(*a*) Unilateral Relief in Respect of Foreign Income Taxed Abroad [Section 91 (1)]

Subject to following conditions unilateral relief is granted in cases where Section 90 is not applicable—

(*a*) Assessee should be resident of India in the previous year;

(*b*) The income, in fact, should have accrued outside India and should not be deemed under any provision of this Act to accrue in India;

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(*c*) The income should be taxed both in India and a foreign country with which India has no agreement for relief against or avoidance of double taxation; and

(*d*) The assessee should have, in fact, paid the tax in such foreign country by deduction or otherwise.

(*b*) Relief in case of Agricultural Income from Pakistan [Section 91(2)]

In case a resident of India has paid any tax on agricultural income which accrued or arose to him during that previous year in Pakistan, he shall be entitled to a deduction from the Indian income tax payable by him of the amount of tax paid in Pakistan or sum calculated at the Indian rate of tax, whichever is less.

Relief in case of Share in the Foreign Income of a Registered Firm [Section 91(3)]

An assessee receiving share in Foreign income of a registered firm shall be entitled to the relief of tax on such share provided the firm receives income from a foreign country with which no agreement exists under section 90 and assessee has paid tax in that foreign country.

Relief will be allowed on doubly assessed income at the rate of the said country or Indian rate of tax, whichever is lower.

QUESTIONS

1. Discuss the provisions of law relating to Double Taxation Relief when an agreement with foreign country exists ?
2. Can a person claim Double Taxation Relief if he has income from a country with which no agreement exists ?

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4 Special Provisions Relating to Avoidance of Tax

This chapter relates to the powers of Assessing Officer regarding computation of income in certain transactions in which a person has tried to avoid tax.

I. Income from transactions with non-resident [Section 92]

When there are business transactions between residents and non-residents and these are so arranged that either the profit from such transactions is nil or is less than the ordinary profits which might be expected in such business. The Assessing Officer shall determine reasonable amount of profit which is deemed to be received and such amount shall be included in the total income.

The Rule 10 of the Income-tax Rules 1962 provides the following guidelines for Assessing Officer to compute the deemed profits u/s 92:

(*i*) Such percentage of turnover, as the Assessing Officer may consider to be reasonable, as the profit accruing or arising from such business transaction.

(*ii*) Proportionate amount of profits (calculated in fallowing manner) shall be deemed as income from such transaction.

$$\text{Deemed Income} = \text{Total Profits} \times \frac{\text{Receipts from such transaction}}{\text{Total receipts of the business}}$$

'Total Profits' shall mean the profits calculated as per provisions of the Income-tax Act.

(*iii*) Any other manner as the Assessing Officer may deem fit, can be used to determine income from such transactions.

II. Avoidance of tax due to transaction resulting in transfer of income [Section 93]

1. Where a person directly or due to associated operations acquires any rights which results in a power for him to enjoy the income of a non-resident (at present or in future) without paying any tax, such income shall be included in his income as if such income would have accrued to him had be not arranged the transfer of assets to non-resident.
2. The above mentioned rule shall also be applicable for any capital sum received regarding these assets.
3. In case any income is deemed as income of a person, such income shall not again be deemed to form part of his income.

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4. The above provisions will not be applicable if Assessing Officer is satisfy that the transactions or associated operation were not made with the object of avoiding tax or if assesse can prove that the transactions or associated operations were *bonafide* commercial transaction.
5. A person shall be deemed to have power to enjoy income of a non-resident if
   (*a*) The income is dealt within such a manner that it ensures a benefit for the resident.
   (*b*) The receipt or accrual of income increases the value of any asset held by him or for his benefit ; or
   (*c*) The assesse receives or is entitled to receive any benefit out of the income or moneys which are subject to such associated operations;
   (*d*) The assessee has the power by means of exercise of power of attornment or power of revocation, as a result of which he can enjoy the income, or
   (*e*) the assessee is in position to control the application of income directly or indirectly.
6. The term '*asset*' shall include property or rights of any kind
7. The term '*associated operations*' shall include an operation of any kind effected by any person in relation to—
   (*i*) any of the asset transferred; or
   (*ii*) any asset representing directly or indirectly, any of the assets transferred, or
   (*iii*) income arising from such assets; or
   (*iv*) any asset representing the accumulation of income of these assets.

Avoidance of tax by certain transactions in securities [Bond Washing] [Section 94]

1. In case a person sells his securities to another person a few days before the accrual of interest and purchases them back after the date of accrual, and Assessing Officer is satisfied that the transaction has been made with the intention of avoiding tax, such interest shall be deemed as income of the transferor and not transferee.
2. In case a person has any beneficial interest in any securities and as a result of some arrangement either no income is received by such person or the income received by him is lower than the amount which he would have received, the interest, which would have accrued on such securities had there been no such arrangement, would be included in the income of person making such arrangement.
3. The above provisions will not be applicable, if such person proves to the satisfaction of the Assessing Officer that the transaction has not resulted into any avoidance of tax or if at all there was some avoidance it was exceptional as there had not been any avoidance of tax in any of three preceding previous years.

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4. In case of dealer of securities, if there is a transaction of sale or purchase of securities and as a result the interest becomes receivable by him but is not deemed to be his income due to the above provisions, no account shall be taken of the transaction in computing profits arising from or loss sustained in this business.
5. The Assessing Officer may direct any person to furnish a detail of securities held by him by serving upon him a notice for not less than 28 days.

QUESTIONS

1. What are those circumstances in which Assessing Officer can take the action to determine income from transaction with non-residents to avoid tax.
2. Explain 'Bond Washing'. How can Assessing Officer include interest on securities received by transferee in the income of transferor ?

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5 COMPUTATION OF TAX LIABILITY

System of taxation—Rounding of Income—Rounding of Tax—illustrations—questions.

System of taxation: In the field of taxation, there are two widely accepted systems of computation of the income-tax namely—

(*i*) Step system, and

(*ii*) Slab system,

Step System. Under this system assessee's income is divided in different groups, and for each group, the rate of tax is prescribed. The rate of tax of that step shall be applicable on the assessee's total income in which step the total income of the assessee falls. It means the rate of highest step (according to assessee's income) is applied on the assessee's total income.

This system is based on the principle that the person with lower income should pay tax at the lower rate. This system is considered to be non-productive. This system is in force in so many countries of the world but it was discontinued in India after 31st March 1939.

This system is explained with the help of the following example:

Suppose the rates are—

(1)	Income up to Rs. 5,000		NIL
(2)	Income between	Rs. 5,000—10,000	10%
(3)	" "	Rs. 10,000— 20,000	15%
(4)	" "	Rs. 20,000—30,000	20%
(5)	" "	Rs. 30,000—40,000	25%
(6)	" "	Rs. 40,000—50,000	30%
(7)	" "	Rs. 50,000—1,00,000	50%
(8)	" above	Rs. 1 lakh	65%

Supposing assessee's total income is Rs. 39,000.

Now assessee's income falls in the step where the rate is 25%. This rate of 25% shall be applicable on the total income of the assessee, which is Rs. 39,000.

So tax will be $= \frac{39,000 \times 25}{100} = 9,750.$

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Slab System. This system of taxation is prevalent in majority of countries and it is also in force in India. This system is considered to be more reasonable, just and equitable.

Under this system total income of the assessee is divided in different slabs. Different rates are prescribed for different slabs: it means a separate rate for each slab and with each successive slab, the rate goes up.

The assessee's income is divided in different slabs and slab-wise rate is applied.

Example

Supposing the rate of tax slab-wise is the same as given in the step system and assessee's income is Rs. 39,000.

Slab			Rate	Tax
Income upto	Rs.	5,000	NIL	NIL
Income between	Rs.	5,000—10,000	10%	500
" "	Rs.	10,000—20,000	15%	1,500
" "	Rs.	20,000—30,000	20%	2,000
" "	Rs.	30,000—40,000		
(*i.e.* Rs. 9,000 in this case)			25%	2,250
Total Tax				6,250

Rounding of Income [Section 288A]

The amount of total income computed in accordance with the provisions of Income-tax Act, shall be rounded off to the nearest multiple of Rs. 10. While doing so, any part of a rupee consisting of *Paise* shall be ignored. Thereafter if such amount is not a multiple of 10, then, if the last figure in the total income of the assessee is five or more, the figure shall be increased to the next higher figure which should be multiple of 10 and if the last figure is less than five, the amount shall be reduced to the next lower amount which is multiple of 10.

So the total income should always be converted into a multiple of ten and the new amount so rounded off shall be deemed to be the total income of the assessee for tax purposes.

Rounding off Tax etc. [Section 288B]

The amount of tax including tax deductible at source or payable in advance, interest, penalty fine or any other sum payable and the amount of refund due shall be rounded off to the nearest rupee. In this process of rounding off, where such amount is in a part of a rupee consisting of paise, then if such is 50 p. or more, it shall be increased to one rupee and if such part is less than 50 p. it shall be ignored.

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Illustration 1. Following are the particulars of income of Mr. Karan for the year ending on 31st March, 1997:

		Rs.
(*a*)	Interest on Government securities (Gross)	600
(*b*)	Interest from Bank Deposits	3,500
(*c*)	Rental value from House Property (Municipal Taxes being Rs. 750)	4,000
(*d*)	Profits of retail cloth business	30,000
(*e*)	1/10th share in an AOP [PFAOP has no such partner whose individual income exceeds Rs. 40,000]	10,000
(*f*)	Dividends from co-operative societies	2,600
(*g*)	Dividends received from Indian Companies (Tax deducted at source @ 20%)	2,160
(*h*)	Dividends out of agricultural income of an Indian Company	600
(*i*)	Interest on debentures of Coop. society	300

He is insured for Rs. 10,000 and paid an insurance premium of Rs. 1,500. He donated Rs. 2,000 to a school (recognised) in which his son is studying.

Compute his total income and tax payable.

Solution

Computation of Total Income of Mr. Karan

	Rs.	Rs.
Income From House Property		
Rental Value	4,000	
Less: Municipal Taxes	750	
A.V.	3,250	
Less; 1/5th of A.V. being Repairs	650	
		2,600
Business Income		
Profit from Cloth Business	30,000	
1/10 share of Profit from AOP	10,000	
		40,000
Income from Other Sources		
Interest on Govt. Securities	600	
Interest on Bank Deposits	3,500	
Dividend from Indian companies [2,160 × 100/80]	2,700	
Dividend from Co-operative Societies	2,600	
Dividend from an Agricultural Company	600	
Interest on debentures of Coop. society	300	
		10,300
Gross Total Income		52,900

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Deductions:

u/s 80L : Income from certain investments	10,300	
u/s 80G : Donations Rs. 2,000; [within 10% of G. Tax. I.] Rate 50% [52,900] – (10,300 + 10,000) 3,200]	1,000	
		11,300
Total Income		41,600

Note 1. Rebate entitlement at average rate u/s 86 on share of Profit from A.O.P.
2. Q.A. for rebate of tax u/s 88: Life Insurance Premium Rs. 15,000

Computation of tax Liability

		Rs.
Total Income=Rs. 41,600		
First Rs. 40,000	NIL	NIL
Rest Rs. 1,600	15%	240
	Tax	240
(*i*) Rebate of tax u/s 86 not allowed as individual income does not exceed Rs. 40,000		NIL
		240
(*ii*) Rebate of tax u/s 88: 20% of Q.A. (1,500 × 20%) Rs. 300 but restricted to		240
Net Tax		NIL
Less: Tax deducted at source on dividends (2,700 – 2,160)		540
Refundable Amount		540

Illustration 2. Compute tax liability of S. Tirath Singh a physically handicapped person for the assessment year 1997-98 from particulars given below :—

	Rs.
(*i*) Professional Gain	1,20,000
(*ii*) Income from House Property (Computed)	6,000
(*iii*) Short term Capital Gain	6,000
(*iv*) Long term Capital Gain	20,000
(*v*) Panjab State Lottery Prize	50,000
(*vi*) Agricultural Income (Net)	20,000
(*vii*) Amount invested in NSC VIII issue	30,000

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Solution : *Computation of total income*

		Rs.
House Property		6,000
P & G : Professional Gain		1,20,000
Capital Gain		
Short term Capital Gain		6,000
Long term Capital Gain		20,000
Other Sources		
Lottery Winnings	Rs. 50,000	
Less exemption u/s 10(3)	5,000	
		45,000
Gross Total Income		1,97,000
Deduction u/s 80U : Physically handicapped		40,000
Total Income		1,57,000

Computation of Tax

			Rs.
(*a*) On Long term Capital Gains of Rs. 20,000 20%			4,000
(*b*) On Lottery prize [Rs. 45,000 × 40%]			18,000
(*c*) On balance total income after integration			
(*i*) Balance Total incomes 92,000 + Agri. Income Rs. 20,000 = 1,12,000			
(*ii*) Tax on Rs. 1,12,000			
on Rs. 60,000 =	3,000		
on Rs. 52,000 = 30%	15,600		
		18,600	
(*iii*) Tax on exempted limit + Agri. income [40,000 + 20,000] = 60,000		3,000	
			15,600
Tax on total income			37,600
Less: Rebate of tax u/s 88			
Q.A. (NSC VIII issue) Rs. 30,000 @ 20%			6,000
Net Tax Payable			31,600

Illustration 3. Mr. Y. Karta of H.U.F., is carrying on the business of publication of books under the name 'Y and Sons Publishers'. The business was started in 1987-88. Calculate the total income of H.U.F. and tax payable by it for the assessment year 1997-98 from the particulars of income given below:

	Rs.
(*i*) Net profit from publication business	56,000

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(*ii*) He invested Rs. 10,000 out of H.U.F. income for acquiring units of eligible issue of a mutual fund (approved u/s 88)

(*iii*) Sale price of house property sold on 5-4-96 for Rs. 1,80,000. House was acquired in 1988-89 at the cost of Rs. 80,000. [C.I.I. for 1988-89 is 161 and for 1996-97 is 305]

(*iv*) Life Insurance Premia: Self Rs. 3,000 p.a.
Wife Rs. 2,000 p.a.
Married Son Rs. 1,000 p.a
Daughter Rs. 1,200 p.a.

(*v*) Dividend from units of U.T.I 3,500

(*vi*) Income from Mutual Fund Scheme 2,200

(*vii*) Dividend from Indian Company (Gross) 3,000

(*viii*) Bank Interest 2,300

Tax deducted at source from dividends is Rs. 600 and advance tax paid is Rs. 10,000. Y's Brother Z is working as manager in a Company getting Rs. 5,000 p.m. as salary. He has also deposited Rs. 45,000 in Public Provident Fund during 1996-97.

Solution

Computation of Total Income of H.U.F.

	Rs.	Rs.
Business Income		
Net profit from Publication business		56,000
Capital Gains: Sale Price	1,80,000	
Cost Price [80,000 × 305/161]	1,51,553	
Long Term Capital Gain		28,447
Income from Other Sources		
Dividend from Units of UTI	3,500	
Income from Mutual Fund	2,200	
Bank Interest	2,300	
Dividend from Indian Companies	3,000	
		11,000
Gross Total Income		95,447
Deductions u/s 80		
(*i*) *u/s 80L* : Bank Interest	2,300	
Dividend on U.T.I.	3,500	
Income from Mutual Fund	2,200	
Company Dividend	3,000	
		11,000
Total Income		84,447

Rounded off to Rs. 84,450

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Computation of tax		Rs.
Tax on Long Term Capital Gains (20% of Rs. 28,450]		5,690
Tax on balance total income [84,450 – 28,450 = 56,000]	Rs.	
First Rs. 40,000 – Nil –	Nil	
Next Rs. 16,000 – 15%	2,400	2,400
		8,090

Less: Rebate of Tax u/s 88: Q.A.		Rs.
Life Insurance Premium		
Self		3,000
Wife		2,000
Married Son		1,000
Daughter		1,200
Amount invested in units		10,000
Amount deposited in P.P.F.		45,000
Q.A. (Restricted to Rs. 60,000)		62,200
Rebate u/s 88 : 20% of Rs. 60,000 = Rs. 12,000 but restricted to tax on regular income		2,400
		5,680
Less: Tax deducted at Source	600	
Advance Tax Deposited	10,000	
		10,600
Refundable amount		4,910

Illustration 4. From the following particulars, compute the total income of firm assessed as AOP and partners. Also compute tax liability of partners.

Profit and Loss Account of the Firm A & B Bros. for the year ending 31-3-97

(A & B are two equal partners in the firm)

To Business Expenses	15,000	By Gross Profit	80,000
To Rent of Premises	4,800	By Bad Debts recovered but allowed earlier	3,000
To Interest on loan taken from Bank	1,400	By Interest on Securities	6,000
To Interest on Capital			
A	3,000		
B	2,000		

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To Salary to A		2,400		
To Commission to B		1,600		
To Profit A	29,400			
B	29,400			
		58,800		
Total		89,000	Total	89,000

Depreciation allowable during the year amount to Rs. 2,000. Individual income of partners A and B is Rs. 26,200 and 31,000 respectively.

Solution

FIRM ASSESSED AS AN AOP (PF AOP)

I. Computation of Firm's Business Profit			Rs.	Rs.
Profit as per P. & L. A/c				58,800
Add: inadmissible deductions:				
Interest on capital	A		3,000	
	B		2,000	
Salary to	A		2,400	
Commission to	B		1,600	
				9,000
				67,800
Less: Allowable depreciation				2,000
				65,800
Less: Income not taxable under this head				
Int. on securities				6,000
Business Profit				59,800
II. Computation of Firm's Total Income				
Business Profit				59,800
Other Sources : Interest on securities				6,000
Total Income				65,800
III. Allocation of Total Income			A	B
			Rs.	Rs.
Interest on Capital			3,000	2,000
Salary			2,400	
Commission				1,600
Share of Profit (65,800–9,000) = 56,800			28,400	28,400
			33,800	32,000

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Total Income of each partner and tax payable by them

		A		B
Other Incomes		26,200		31,000
Share from firm assessed as AOP		33,800		32,000
Total Income		60,000		63,000
Tax Payable	Rs.			Rs.
First Rs. 40,000 of total income	NIL			NIL
Next Rs. 20,000 of total income –15%	3,000			3,000
On Balance of total income 30%	NIL			900
	3,000			3,900
Less rebate of tax at average rate on share from firm assessed as AOP 5%	1,690	6.19%		1,981
Net Tax	1,310			1,919

Q. No. 1

Compute the tax liability of Mr. A for the assessment year 1997-98 if his total income is (*a*) Rs. 21,670 (*b*) Rs. 44,371 (*c*) Rs. 111,549

[**Hints**: (*a*) NIL (*b*) Rs. 656 (*c*) Rs 17,965]

Q. No. 2

Compute the tax liability of a H.U.F. (which has at least one member whose individual income exceeds Rs. 40,000) if its total income is (*a*) Rs. 24,640 (*b*) Rs. 80,569 ?

[**Hints:** (*a*) Rs. Nil (*b*) Rs. 9,171]

Q. No. 3

Compute the tax liability of an individual from figures given below :

(*i*) Gross Salary Rs. 65,000
(*ii*) House Property Rent Rs. 20,000
(*iii*) Long Term Capital Gains Rs. 20,000
(*iv*) Winning from Loterry Rs. 50,000 (1-11-96)
(*v*) Qualifying amount for rebate of tax u/s 88 Rs. 50,000

[**Hints :** Total Tax Rs. 26,800; Less rebate u/s 88 Rs. 10,000 Tax Payable Rs. 16,800]

Q. No. 4

Compute tax liability from the particulars given below for the assessment year 1997-98 if :—

(*a*) assessee is an individual;
(*b*) assessee is an H.U.F. which has atleast one such member whose individual income exceeds Rs. 40,000;

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(*c*) assessee is a partnership firm assessed as firm (PFAF) :

	Rs.
(*i*) Business Income	1,04,300
(*ii*) Long term Capital Gain	30,000
(*iii*) Race Winnings (Horses)	10,000
(*iv*) Amount deposited in PPF	20,000
(*v*) NSC VIII issue purchased	10,000

[**Hints :** (*a*) Individual and (*b*) H.U.F. Tax Rs. 25,290 Rebate u/s 88 Rs. 6,000 Net Tax 19,290; (*c*) PFAF—Tax Rs. 50,720 No rebate of tax u/s 88]

Q. No. 5

Compute tax liability of Mrs. Jaya for the assessment year 1997-98 from the particulars given below :—

	Rs.
(*i*) Gross salary	80,000 p.a.
(*ii*) Self occupied house whose ARV is	18,000 p.a.
Municipal Taxes	2,000 p.a.
Interest on loan for construction of house	12,000
Amount repaid against loan taken from HDFC	15,000
(*iii*) Bank Interest	6,000
Interest on Debentures	4,000
Interest on Govt. securities	4,000
Interest accrued on NSC VIII issue	1,240
(*iv*) Amount contributed to RPF	4,800
Life Insurance premium on a policy of 30,000	4,000
Amount deposited with P.P.F.	4,000
(*v*) Tax deducted at source from salary	2,400

[**Hints :** Standard Deduction Rs. 18,000; HP loss (–) 10,000 other sources Rs. 15,240 GTI 67,240 80L 11,240 Total Income 56,000 Tax Rs. 2,400 Rebate u/s 88 Rs. 4,808 but restricted to actual tax of Rs. 2,400 Refund due Rs. 2,400]

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PART IV

ASSESSMENTS

1. ASSESSMENT OF INDIVIDUALS
2. ASSESSMENT OF H.U.F.
3. ASSESSMENT OF FIRMS
4. ASSESSMENT OF COMPANIES
5. ASSESSMENT OF CO-OPERATIVE SOCIETIES
6. ASSESSMENT IN SPECIAL CASES
7. PRESUMPTIVE ASSESSMENT FOR RETAIL TRADERS

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1 ASSESSMENT OF INDIVIDUALS

Treatment of income received from certain other institutions—income of other persons to be added in the income of individual—illustrations and questions.

Section 4 of Income-tax Act, 1961 read with section 2 (31) provides the different units of assessment. These are:

(*i*) Individual
(*ii*) Hindu Undivided Family (H.U.F)
(*iii*) Firm
(*iv*) Association of persons or a body of Individuals
(*v*) Local authority
(*vi*) Company
(*vii*) Artificial Juridical person.

'Individual' includes both male and female assessee. Every 'individual' is supposed to pay tax on his or her total income at a graded scale of tax rates ruling during that assessment year. In addition to his own income some incomes received by him in some other capacity and some incomes although received by other persons are to be included in his total income.

Income received from different institutions

1. *As a member of Hindu Undivided Family.* Any sum received by an individual as a member of H.U.F. out of family income is not to be included in his total income, because the share of income received from the H.U.F. is exempted in the hands of such individual, the family may or may not have paid tax on that income [Section 10 (2)].

If the member earns his own income, besides being the member of H.U.F. he will pay tax on his own earned income.

But u/s 64 (2) where an individual converts his individual property into the common pool of H.U.F. of which he is a member, income from such property shall be included in his individual income.

2. *Share of income from AOP or PFAOP*

(*a*) In case AOP or PFAOP's income does not exceed Rs. 40,000 .....share from such AOP/PFAOP shall be fully added in individual income and shall be fully taxable.

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(*b*) If total income of any member/partner of AOP/PFAOP exceeds Rs. 40,000; or is taxable at a rate higher than MMR (*i.e.* 40%)

—The AOP/PFAOP shall pay tax at MMR *i.e.* 40%. Share of income from such AOP/PFAOP shall not be added in individual income of partners and as such shall be fully exempted.

(*c*) If total income of all of its members does not exceed Rs. 40,000, AOP/PFAOP shall pay tax at the rates applicable to an individual and share of income from such AOP/PFAOP shall be fully added in individual income of partners. Such share shall be eligible for rebate of tax at average rate u/s 86.

(*d*) Share of loss from AOP/PFAOP cannot be adjusted from individual income.

3. *As a partner of firm assessed as firm.* The share received by an individual from a firm (PFAF) shall not be included in his total income irrespective of the fact, whether the firm has paid the tax or not. Any salary or other remuneration and interest on capital is taxable under the head Profits and Gains.

4. *As a shareholder of a company.* The gross amount of dividend received by an individual is to be included in his total income. The gross amount means, the net dividend received plus tax deducted at source. The shareholder is liable to pay tax on whole of his income from dividend i.e., the gross amount of dividend declared by the company. The assessee shall get credit of the tax deducted at source out of his final tax liability. The individual shall be entitled to the deduction as provided by the different sections of Income-tax Act.

> With effect from assessment year 1998-99 dividend received from Indian companies shall be fully exempted and shall not form part of total income.

Income of other persons to be included in the Total Income of an individual

Under the provisions of section 60 to 64 of the Income-tax Act, 1961, in the following cases some incomes although accruing to other persons, but to prevent tax-evasions, are included in the total income of individual assessee.

1. *Transfer of income without transfer of asset.* The income shall be included in the total income of transferor.

2. *Revocable transfer of assets.* The income from such assets is also included in the total income of the transferor. If the asset is not revocable during the life time of the transferor, it shall be regarded as irrevocable transfer for this purpose.

3. *Income of a minor child.* With effect from assessment year 1993-94 income of a minor from whatsoever sources shall be added in the income of that parent whose other income is higher. In case income is included in the income of one parent it shall always be included in the income of that parent. Income of a minor handicapped or mentally retarded child shall not be clubbed.

4. *Income from assets transferred to the spouse, daughter-in-law by an individual* without adequate consideration shall be included in the income of that individual. The relationship must exist on the date on which asset is transferred. On a particular

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date on which transferor and transferee have no relationship with each other, but subsequently such relationship is formed, the income from such asset shall remain to be the income of transferee.

5. *Income from the assets transferred by an individual.* Where the assets are transferred by an individual in such a way that the benefits of assets accrue directly or indirectly to the spouse or minor child of the transferor, the income from such transferred assets shall be included in the total income of the transferor.

6. *Share of income arising to spouse for being member of a trust or to minor child who is beneficiary under a trust.* The Finance Act, 1979 provides that any income arising to the spouse or minor child from a trust shall be deemed to be the income accruing indirectly to the spouse or minor child of such individual from the membership of the spouse to or from the admission of minor to the benefits of a firm in which such individual is partner.

The above mentioned provisions have already been explained in detail in the chapter "Aggregation of Income" in Part II.

COMPUTATION OF TAX LIABILITY

After computing the total income, next step is to compute the tax liability. Detailed treatment of computation of tax and rates of tax are given in Chapter 5 part III of this book. Briefly these steps are:

1. Round off total income to nearest multiple of 10.
2. Divide the total income into three parts:
   (*a*) *Long term capital gain.* Calculate tax at the rate of 20%.
   (*b*) *Winning from lotteries, puzzles, races, cardgames, gambling and betting.* Calculate tax at the rate of 40%.
   (*c*) *Balance total income.* Calculate tax at scheduled rates.
3. Compute tax in the manner given above.
4. Out of tax so calculated rebates of tax u/s 86, 89(1) 88 and 88B are allowed. Balance is net tax payable.

Illustration 1. From the particulars given below, compute the total income and tax payable of Mr. Deb, a resident of Chandigarh:

I.	(1) Salary	4,000 p.m
	(2) T.A. Bill	5,000 p.a
	Actual Expenditure	6,000 p.a
	(3) His contribution to Statutory Provident Fund	300 p.m
	(4) Employer's contribution to S.P.F.	10% of salary
	(5) Interest on accumulated Balance of S.P.F. @ 13%	2,000

II. He owns two houses, one of which is let out at a rent of Rs. 400 p.m. and other (whose annual value is Rs. 1,000) remained vacant throughout

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the year on account of his employment at Ambala where he has taken a house on rent. The two houses are subject to Municipal Taxes of Rs. 600 and 100 respectively.

III. He received Rs. 1,500 (gross) as interest from the Government securities and Rs. 11,600 as gross dividend.

He pays Life Insurance premium of Rs. 5,000 on his life policy of Rs. 40,000. He deposited Rs. 250 p.m in Post Office C.T.D. 10 year account.

Solution

Computation of Total Income of Mr. L for the current assessment year.

	Rs.	Rs.
I. *Income from Salary*		
(*i*) Salary @ Rs. 4,000 p.m.	48,000	
(*ii*) Travelling Allowance—Exempted	—	
Gross Salary	48,000	
Standard deduction u/s 16 (*i*) (33.33%)	16,000	
		32,000
II. *Income from House Property*		
Rent of let out house	4,800	
Less: Municipal Taxes	600	
Annual Value	4,200	
Deduction:		
1/5th of A.V. as repairs	840	
		3,360
The other house is exempted u/s 23 (2)		
III. *Income from other sources*		
Dividend (Gross)	11,600	
Interest on Govt. securities	1,500	
		13,100
Gross Total Income		48,460
Deduction u/s 80L : Dividend	11,600	
Interest on Government Securities	1,500	
		13,100
Total Income		35,360

Note: Q.A. for rebate u/s 88

(*i*) Contribution to S.P.F.	3,600
(*ii*) Premium of Life Insurance	5,000
(*iii*) Contribution to P.O.C.T.D. A/c	3,000
Q.A.	11,600

Tax Liability--Nil as total income does not exceed the exempted limit of Rs. 40,000

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Illustration 2. The following particulars are given by M.D. Mathur, Madras, in respect of his annual income for the year ended 31st March 1997:

(*i*) Consolidated salary till 30-9-1996 at Rs. 3,500 p.m. and from 1-10-1996 Rs. 4,000 p.m.

(*ii*) House rent allowance at 20% of salary.

(*iii*) Actual house rent paid Rs. 1,500 p.m.

(*iv*) Contribution to recognised Provident Fund by self and employer- each 10% of salary.

(*v*) Life Insurance Premium paid Rs. 1,200. (Sum assured Rs. 10,000).

(*vi*) Leave Travel Allowance received Rs. 2,600, Rs. 2,000 was spent on travel to home district.

(*vii*) Interest and dividend incomes:

	Rs.
Interest on Term Deposits with Punjab National Bank	6,000
Income from units of Unit Trust of India	3,000
Interest on debentures of Ponds India Ltd.	1,750
Dividend from equity shares	5,000

(*viii*) Medical expenses incurred in treatment of self and family Rs. 5,000. His employer reimbursed Rs. 2,500.

(*ix*) Rent received from tenant of own house property Rs. 9,600. Municipal taxes paid Rs. 600.

Prepare Mathur's statement of income showing computation of taxable income giving such explanation as necessary and tax liability. Salary is due on last date of the month. *(B.Com., P.U. April, 1993)*

Solution

Computation of total income of Mr. M.D. Mathur for the assessment year 1997-98

			Rs.	Rs.
I.	*Salaries*			
	Salary (1-4-96 to 30-9-96 @ 3,500 p.m			
	1-10-96 to 31-3-97 @ 4,000 p.m)			45,000
	House Rent allowance Received		9,000	
	Less exempted u/s 10 (13 A)			
	(*i*) Actual HRA received	Rs. 9,000		
	(*ii*) Rent paid (–) 10% of salary (18,000 – 4,500)	13,500		
	(*iii*) 50% of salary	22,500		
	Least Exempted		9,000	
	Taxable HRA			NIL
	Employer's contribution exempted as it is less than 10% of salary			NIL
	Excess of Leave Travel Allowance over actual expenditure (Rs. 2,600 – Rs. 2,000)			600
	Reimbursement of Medical Expenses (Exempted)			NIL

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Gross salary			45,600
Standard Deduction u/s 16 (i) (33.33%)			15,200
Salary Income			30,400
II. *House property* A.R.V.		9,600	
Less: Taxes		600	
Net A.V.		9,000	
Less: 1/5th for repairs		1,800	
			7,200
III. *Income from Other Sources*			
Interest on Bank Deposit		6,000	
Income from Units of U.T.I.		3,000	
Dividend on Equity Shares		5,000	
Interest on debentures		1,750	
			15,750
Gross Total Income			53,350
Deduction u/s 80 L			
Income from Units of U.T.I.	3,000		
Dividend from shares	5,000		
Bank Interest	6,000		
			14,000
Total Income			39,350

Note: Q.A. for rebate of tax u/s 88

	Rs.
(*a*) Own contribution to R.P.F.	4,500
(*b*) Life Insurance Premium	1,200
	5,700
Tax liability on total income of Rs. 39,350	NIL

Illustration 3. The following are particulars of the Income of the University teacher during the year ending 31st March 1997:

(*a*) Salary Rs. 4,200 per month from which 10 per cent is deducted for provident fund to which the University contributes 12 per cent.
(*b*) Rent-free bungalow of the annual letting value of Rs. 3,960.
(*c*) Wardenship allowance Rs. 1,200 per annum.
(*d*) 9% interest on Government Loan of Rs. 15,000.
(*e*) Income from house property (computed) Rs. 1,800.

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(*f*) Interest on postal saving bank deposit Rs. 300.

(*g*) Interest (gross) Rs. 2,500.

(*h*) Examinership remuneration Rs. 3,500.

During the year he paid Rs. 2,400 as life insurance premium on his own policies and spent Rs. 600 on books purchased for his own use.

Find out his Total Income, tax and exempted income.

Solution

	Rs.	Rs.
Salary Income		
Pay @ Rs. 4,200 p.m.		50,400
Wardenship allowance @ 100 p.m.		1,200
Value of Rent-free Accommodation:		
F.R.V. 3,960 or 10% of Salary i.e. (50,400 + 1,200) whichever is less		3,960
Gross Salary		55,560
Standard Deduction u/s 16 (i)		18,000
Salary Income		37,560
Income from House Property (Computed)		1,800
Income from other sources		
Interest (gross)	2,500	
Examinership Remuneration	3,500	
Interest on Govt. Loan	1,350	
		7,350
Gross Total Income		46,710
Deduction u/s 80 L		
Interest on Govt. Securities		1,350
Total Income		45,360

Note: Q.A. for rebate of tax u/s 88	Rs.
(*a*) Own contribution to S.P.F.	5,040
(*b*) Life Insurance premium	2,400
Q.A.	7,440

Computation of tax on total income of Rs. 45,360

		Rs.
On first Rs. 40,000 of total income	NIL	NIL
On next Rs. 5,360 of total income	15%	804
	Tax	804
Less: rebate of tax u/s 88		
Q.A. Rs. 7,440 @ 20% but restricted to tax payable		804
Tax payable		NIL

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Illustration 4. Dr. Singh is a practitioner. Besides his own practice, he works as a part-time physician in a private hospital for which he receives a monthly remuneration. He is also Consultant-Physician of ABC Co. Ltd. on a monthy retainer fee.

The doctor maintains a record of his receipts and payments and for the year ended 31st March, 1997 the following information is abstracted therefrom:

	Rs.
Receipts:	
Consultation fee receipts	70,000
Gross Remuneration from the private hospital	30,000
Retainer fee from ABC Co. Ltd.	10,000
Interest on bank deposits (nationalised bank)	12,000
Payments:	
Rent and electricity charges for the clinic	17,000
Telephone charges	7,400
Printing and stationery	500
Car maintenance expenses	9,000
Wages of clinical assistant	6,600
Driver's salary	3,600
Life Insurance premium	2,400

The written down value of the car purchased in January 1990 and the furniture at the clinic as on 1-4-1996 are noted to be Rs. 40,000 and Rs. 3,000 respectively. 30% of the use of the car and the telephone is attributable to personal and private purposes.

Prepare a statement showing the total income and tax payable of the doctor for the assessment year 1997-98.

Solution

Computation of Total Income of Dr. Singh.

	Rs.	Rs.	Rs.
I. *Salary*			
Salary from private Hospital	30,000		
Less: Standard Deduction 33$^1/_3$% of 30,000 or Rs. 18,000 w.e. is less	10,000		
Salary Income			20,000
II. *Professional Gain*			
Receipts			
Consultation fee	70,000		
Retainer fee	10,000		
		80,000	
Less expenses:			
Rent & Electricity	17,000		
Telephone (7,400 less 30% for personal use 2,220)	5,180		
Printing & stationary	500		

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Wages of clinical Assistant		6,600	
Car maintenance (9,000 less 30% for personal use: 2,700)		6,300	
Driver's salary (3,600 less 30% for personal use 1,080)		2,520	
Depreciation of car (40,000 × 25%)	Rs. 10,000		
Less: 30% for personal use	3,000		
		7,000	
Depreciation on furniture (10% of Rs. 3,000)		300	
			45,400
			34,600
III. *Other sources*			
Interest on Bank Deposit			12,000
Gross Total Income			66,600
Deductions :			
u/s 80L: Bank Interest Rs. 12,000			12,000
Total Income			54,600

Note: Q.A. for rebate of tax u/s 88: L.I Premium Rs. 2,400.

Computation of tax on total income of Rs. 54,600		Rs.
On first Rs. 40,000 of total income	NIL	NIL
On next Rs. 14,600 of total income	15%	2,190
	Tax	2,190
Less: rebate of tax u/s 88 Q.A. Rs. 2,400 @ 20%		480
	Tax payable	1,710

Illustration 5. From the following Receipts and Payments Account for the year ended 31st March 1997 of Dr. Deb and from further particulars given below, compute his total income and tax payable.

Receipts	Rs.	*Payments*	Rs.
To Opening cash balance	10,000	By Consulting Room Expenses	12,000
,, Consultation fees	50,000	,, Cost of X-ray machine	60,000
,, Salary from medical College	66,000	,, Car Expenses	6,000
,, Sales of shares	10,000	,, Life Insurance Premium	2,000
,, Interest from bank	2,000		

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,, Dividends (Gross)	1,200	,, Son's marriage Expenses	5,000
,, Loan from Bank	20,000	,, Advance Income Tax	10,000
,, Cash Gifts on Son's marriage	10,000	,, Household Expenses	72,000
		,, Closing Cash Balance	2,200
	1,69,200		1,69,200

Particulars:

(*i*) 1/2 of car expenses are treated as personal.

(*ii*) Cost of shares acquired in 1988-89 was Rs. 5,000.

(*iii*) He deposited Rs. 35,000 in P.P.F. on 30.3.97.

Solution

Computation of Total Income of Dr. Deb for the current assessment year.

	Rs.	Rs.
I. *Income from salary:*		
Salary from Medical College	66,000	
Less: Standard Deduction @ 33 1/3% or Rs. 15,000 whichever is less.	15,000	
		51,000
II. *Professional Income:*		
Professional Receipts:		
Consultation fees	50,000	
Less: Professional Expenses:	Rs.	
Consultation Room Expenses	12,000	
Depreciation on X-ray machine @ 25% of 60,000	15,000	
Car expenses (1/2 allowable)	3,000	
	30,000	
		20,000
III. *Capital Gains : Long Term*		
Sale price	10,000	
Cost (5,000 × 305/161)	9,472	
Taxable Capital Gain		528
IV. *Other Sources:*		
Interest from Bank	2,000	
Dividend (Gross)	1,200	
		3,200
Gross Total Income		74,728
Deduction:		
U/s 80L: Dividend and Interest		3,200
Total Income		71,528
Rounded off to Rs. 71,530		

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Note 1. No dep. on car as its cost or W.D.V. is not given.

2. *Q.A. for rebate of tax u/s 88*

	Rs.
Life Insurance Premium	2,000
Amount deposited in P.P.F	35,000
Total Q.A.	37,000

Computation of tax on total income of Rs. 71,530	Rs.
(*i*) On long term capital gain of Rs. 530 @ 20%	106
(*ii*) On balance total income [71,530 – 530] Rs. 71,000	
On first Rs. 60,000 of total income	3,000
On balance of Rs. 11,000 @ 30%	3,300
Tax	6,406
Less: rebate of tax u/s 88 Q.A. Rs. 37,000 @ 20% Rs. 7,400 but restricted to tax on [Total income – Long term capital gain]	6,300
Tax Payable	106

Illustration 6. Kishore Kumar is the proprietor of a business. The following was the Profit & Loss Account of his business for the year ended March 31, 1997.

	Rs.		Rs.
To Office Expenses	10,000	By Gross Profit	29,225
To Proprietor's Salary	6,000	By sale of import entitlements	30,000
To General Expenses	7,500	By profit on sale of	
To Bad Debts	1,500	residential house (long term)	
To Advertisement	4,200	indexed	24,000
To Fire Insurance Premium	1,800	By Bad debts recovered	
To Depreciation	3,900	(disallowed earlier by the)	
To Motor Car Expenses	1,500	ITO for want of evidence)	6,000
To Legal Charges for defending a suit for alleged breach of a trading contract	600	By Interest from Govt. securities (net) listed 10%	6,300
		By Dividends (Net) from agricultural companies	2,000
To Donation to Bombay University	2,500	By Interest on Post office Cash certificates and $3^1/_2$%	
To Interest on Proprietors' Capital	1,400	National Saving Certificates	2,475
To Reserve for future losses	5,000	By Income from Horse races (gross)	5,000

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To Income tax paid on last assessment	4,400	
To Life Insurance Premium	4,000	
To Advance Income tax paid	3,600	
To Net Profit	47,100	
	1,05,000	1,05,000

Further information is given :

(*a*) General expenses include Rs. 1,200 paid as compensation to an old employee whose services were terminated as his services were considered detrimental to the profitable conduct of the business and Rs. 200 as help to a poor university student.

(*b*) A sum of Rs. 4,740 being cost of a small machine has been included in general expenses.

(*c*) The advertisement cost includes expenditure Rs. 600 on one wooden show case and Rs. 1,800 on calender and diaries.

(*d*) One-third of Motor Car expenses is for personal use of the car.

(*e*) Depreciation in found to be in excess by Rs. 1,700 compared to the amount allowable under income tax rules.

(*f*) Reserve for future losses represents a demand of Sales-tax under dispute Compute Kishore Kumar's taxable profit and total income for the assessment year 1997-98. [*Panjab B.Com. April, 1996*]

Solution

Computation of total Income of Mr. Kishore Kumar Business Income :

	Rs.	Rs.
Net Profit as per P & L A/c		47,100
Add disallowed expenses :		
Proprietor's salary	6,000	
Donations	2,500	
Interest on capital	1,400	
Reserve for future losses	5,000	
Income tax	4,400	
Life Insurance Premium	4,000	
Advance Income tax	3,600	
Help to a poor student	200	
Cost of a small machine	4,740	
Motor Car expenses (1/3rd)	500	
Excess Depreciation	1,700	
Cost of wooden show case	600	34,640
		81,740

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Less Allowable Depreciation		
On small machine 25% of 4,740	1,185	
On wooden show case 10% of 600	60	
Less Incomes credited but to be treated under other heads :		
Long term capital gain	24,000	1,245
Bad debts recovered (disallowed earlier)	6,000	80,495
Interest on Govt. securities	6,300	
Dividend	2,000	
Interest on Post office sowings Bank A/c	2,475	
Horse race winnings	5,000	45,775
Business Income		34,720

Computation of Total Income

Profits & Gains			
Business Profit			34,720
Capital Gains			
Long term Capital gain			24,000
Other Sources			
Interest on Govt. securities $\left(6{,}300 \times \frac{100}{90}\right)$		7,000	
Dividend (No TDS)		2,000	
P.O.S.B. Interest (Exempted)		NIL	
Race winnings (5,000 – 2,500)		2,500	11,500
Gross Total Income			70,220
Deduction u/s 80			
U/s 80 L :			
Interest on Govt. securities	7,000		
Dividend	2,000	9,000	
U/s 80 G :			
Donations Rs. 2,500			
Q.A. = 2,500 @ 50%		1,250	10,250
Total Income			59,970

Notes :

1. Amount claimed as per demand notice of sales tax cannot be allowed till it is actually paid.
2. No TDS if dividend is paid by a company in which public is substantially interested for an amount not exceeding Rs. 2,500.

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Q. No. 1

Compute the total income of Mr. Ram from the particulars given below:

		Rs.
(*i*)	Interest on Securities (Gross)	7,000
(*ii*)	Rental value of a house Rs. 650 p.m.: Self-acquired but transferred to H.U.F. common pool. Income from this house (computed) is Rs. 2,250.	
(*iii*)	Share from firm assessed as firm in which he has $^1/_3$ rd share—	Rs. 15,000.
(*iv*)	Commission received by his wife from such firm for acting as its selling agent.	Rs. 5,000

[**Hints**: Total income Rs. 14,250; House property u/s 64 (2): 2,250; Share from firm exempted u/s 10(2A) and income from other sources u/s 64 (*i*) (*ii*) 5,000 + 7,000 = 12,000] [P-9]

Q. No. 2

Miss Piyush was born on 6.8.1979. On her engagement on 15.3.96 she received cash gifts of Rs. 30,000 each from her father, father's mother, father's father, mother and mother's mother. All these relatives made similar gifts on the day of her marriage *i.e.* on 1.4.96. The amount so received is deposited in a private limited company in which her husband has substantial interest. During the year 1996-97 she received interest @ 15% *i.e.* Rs. 45,000. Discuss how this income will be assessed to tax. (*C.A. Inter May 1990 Adapted*)

[**Hints** : With effect from assessment year 1993-94 all such incomes which accrues to a minor child shall be included in the income of that parent whose other income is higher. As such full interest of Rs. 45,000 shall be clubbed with the income of that parent whose individual total income is higher. The parent can claim exemption of Rs. 1,500 u/s 10 (32) out of such income].

Q. No. 3

A is a Professor in a Calcutta College getting a salary of Rs. 4,000 p.m. plus 18% on account of dearness allowance. He contributes 8% of his salary to Provident Fund and employer contributes the same amount. He is also hostel warden and has been provided with rent-free unfurnished accommodation whose annual rental value is Rs. 4,000. He owns a house which is let out at Rs. 800 p.m. and he pays municipal taxes amounting to Rs. 1,600 p.a.

During the previous year he received the following incomes:

(*i*) 10% dividend on shares of Rs. 12,000.

(*ii*) 15% dividend on Rs. 20,000 shares of Syndicate Ltd.

(*iii*) 12% interest on debentures of Rs. 15,000.

(*iv*) Rs. 4,600 being one-third share of profits in an A.O.P.

(*v*) Rs. 2,400 dividend from a Company (after deduction of tax @ 20%).

He has insured his life for Rs. 25,000 and paid Rs. 3,250 as annual premium. Ascertain his Total Income and tax payable.

[**Hints**: Salary Income Rs. 45,640; H.P. Rs. 6,400; P. & G. Rs. 4,600; Other Sources Rs. 9,000; Deductions u/s 80 L Rs. 7,200; Total Income Rs. 58,440; Q.A. for rebate u/s 88 Rs. 7,090. Tax Rs. 2,766 less rebate u/s 88 Rs. 1,418 Net tax Rs. 1,348] [P-22]

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Q. No. 4

From the following particulars of income of Shri M. Shaw during the year ending March 31, 1997 ascertain his total income for income-tax purposes.

(*a*) As a secretary of a company, he received salary at Rs. 4,000 per month and a house rent allowance of Rs. 750 per month. He is living in a house for which he pays Rs. 1,000 p.m.

(*b*) He had a house property which was let out at Rs. 1,000 per month for which he had to pay Rs, 500 as ground rent and Rs. 167 as insurance charges. The house was subject to local tax at Rs. 2,000 per year.

(*c*) He owned a residential house since 1965 which he sold during the year at a profit of Rs. 2,500.

(*d*) He had some agricultural lands in the village wherefrom he received an income of Rs. 1,200.

(*e*) During the year he received Rs. 750 as interest from bank and Rs. 50 interest on Postal Saving Bank Account.

(*f*) He was a gambler and during the year he earned an income of Rs. 5,900 from gambling.

(*g*) From a cotton mill his dividend income is Rs. 3,000.

(*h*) He earned Rs. 1,500 as interest (Gross) from Government Securities.

(*i*) He had a half-share in a firm assessed as AOP and his share of profit was Rs. 7,200.

He insured his life and paid Rs. 2,900 as premium and donated Rs. 20,000 for promotion of family planning. *(Adapted I.C.W.A. Final)*

[**Hints** : Salary Income 33,200; H.P. 7,333; P. & G. 7,200; L.T. C.G. 2,500; Other Sources Rs. 6,150, Deduction u/s 80 L 5,250 and 80 G 4,863; Total Income Rs. 46,270 Q.A. for rebate u/s 88 Rs. 2,900] [P-23]

Q. No. 5

Mr. I.M. Verma is the Manager of Punjab Cotton Mills Ltd. He draws a salary of Rs. 4,000 p.m. His other items of income are:

(*a*) Interest on fixed deposits with Andhra Bank Rs. 2,800.

(*b*) Winning from lottery Rs. 65,000.

(*c*) Dividends from an Indian company Rs. (Net) 3,200.

(*d*) Long-term capital gains from the sale of his residential house, occupied for the last 20 years, Rs. 1,15,000. He purchased another house for his residence for Rs. 1,05,000 within four months of the transfer of his residential house.

(*e*) Short term capital loss Rs. 10,000.

(*f*) Long-term capital loss from Gold brought forward from the assessment year 1995-96 Rs. 20,000.

The following deductions are claimed:

(*i*) Life Insurance premium (Policy for Rs. 1,00,000) Rs. 12,500.

(*ii*) Donation for Punjabi University, (Notified as institute of National Eminence) Rs. 10,000.

(*iii*) Education of his children, Rs. 4,500.

Compute his total income for the assessment year 1997-98.

[**Hints**: Salary Income Rs. 32,000; Capital Gains 10,000 S.T.C. Loss to be adjusted 10,000). Other sources 66,800 GTI 98,800 80L Rs. 6,800 80G Rs. 10,000 Total Income Rs. 82,000; Q.A. for rebate of tax u/s 88 Rs. 12,500; Capital loss B/F from 1995-96 to be C/F as current Loss is to be adjusted first.] [P-24]

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Q. No. 6

Given below is the profit and loss account of Shri Rajaram for the year ended 31-3-1997.

Dr.	Rs.	Cr.	Rs.
To Salaries	7,000	By Gross Profit	50,000
" Drawings	8,000	" Interest on Post Office Saving Bank Account	100
" Insurance premium on his life	1,000		
" Depreciation	4,500	" Proceeds from Life Insurance Policy	6,900
" Donation to the recognised institutions	500		
" General expenses	2,600	" Interest on Bank deposits	3,600
" Education expenditure on his three dependent sons in England	6,600		
" Provisions for doubtful debts	1,500		
" Income-tax	2,000		
" Rent	1,700		
" Net profit	25,200		
	60,600		60,600

Compute his taxable income for current assessment year after taking the following information into consideration:

(*a*) The amount of depreciation allowable is Rs. 4,000.

(*b*) General expenses include Rs. 600 for his private expenses.

[**Hints**: Business Income 35,300; Other sources 3,600; G.T.I. 38,900; Deduction, u/s 80G 250 and 80L 3,600; Total Income Rs. 35,050; Q.A for rebate u/s 88 Rs. 1,000] [P-25]

Q. No. 7

The following is the Receipts and Payments Account of Dr. Anand Reddy :

Recipts	Rs.	Payments	Rs.
To Balance on 1.4.1996	11,640	By Rent of the clinic	14,000
" Fees at the clinic	1,80,430	Repairs to clinic	3,360
" Salary received from Medical College	48,000	" Purchase of equipments	3,980
		" Salary paid to staff	64,000
" Life Policy Matured	25,000	" Sundry Expenses	4,470
" Dividend from Indian		" Purchase of medicine	12,700
" Companies (Gross)	2,700	" HDFC	
" Interest (Gross) on :		Housing Loan	16,640
Debentures	4,200	" Interest on Housing Loan	10,000
FD with Companies	2,800	" Taxes—Income-tax	17,900
FD with SBI	3,700	House Property tax	3,000
S.B. with SBI	730	" Investment in Magnum Certificates	30,000

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	"	Contribution to PPF	23,000
	"	Premium on Life Policy	8,510
	"	Deposit in National Savings Scheme 1992	10,000
	"	Loan to a friend	20,000
	"	Personal Expenses	37,000
	"	Balance on 31.3.1997 c/d	640
2,79,200			2,79,200

Dr. Reddy is regularly following 'cash' system of accounting. He stays in a new hosue which he purchased on 31.3.1996. For this purpose he borrowed Rs. 80,000 from Housing Development Finance Corporation Ltd., (HDFC). The annual letting value of the property is Rs. 24,000. Magnum Certificates have been notified under Section 88. Stock of medicine on 31.3.1996 was Rs. 3,400 and on 31.3.1997 was Rs. 2,100. Compute the total income and tax of Dr. Anand Reddy for the year ending 31.3.1997. *(C.A. Inter Adapted)*

[**Hints :** Salary Income Rs. 32,000, HP loss (–) 10,000 Professional Gain Rs. 79,605, Other Sources 14,130 Deduction u/s 80L 7,130 Total Income Rs. 1,08,605 Q.A. for rebate u/s 88 Rs. 61,510 but restricted to Rs. 60,000 Tax Rs. 17,583 rebate restricted to Rs. 12,000 only. Net tax payable Rs. 5,583] [P-15]

Q. No. 8

The following particulars are furnished by Mrs. X, a citizen of India and resident for the purposes of income-tax:

			Rs.
(*a*)	Net salary received after deduction of tax at source and contribution to a recognised Provident Fund		45,000
(*b*)	Tax deducted at source from salary		7,500
(*c*)	Own contribution to the Provident Fund		6,200
(*d*)	Employer's contribution to the Provident Fund		6,200
(*e*)	Interest credited to the Provident Fund @ 13% p.a.		3,900
(*f*)	Travelling expenses for self and husband for proceeding on leave to her home district		2,500
(*g*)	Contribution by the employer to an approved Gratuity Fund		2,100
(*h*)	House-rent allowance (the house is at Calcutta and the rent actually paid amounts to Rs. 8,400)		6,000
(*i*)	Dividends from an Indian Company (net)		8,000
(*j*)	Tax deducted at source from dividend		2,000
(*k*)	Life Insurance Premium:		
	(*i*) On own life-sum assured Rs. 85,000	10,000	
	(*ii*) On husband's life-sum assured Rs. 35,000	2,500	
	(*iii*) On minor child's life—sum assured Rs. 12,000	900	
	Total	13,400	

Compute the Total Income of Mrs. X.

[**Hints:** Salary Income 41,800; Other sources 10,000; G.T.I. 51,800, Deduction u/s. 80L 10,000: Total Income 41,800: Q.A. for rebate u/s 88 Rs. 19,600 Tax Rs. 270 less rebate u/s 88 Rs. 3,920 but restricted to Rs. 270 only Tax Nil]

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Q. No. 9

Sh. Mohan Lal of the Trading Corporation Ltd, Jaipur had the following details of his salary and other incomes in the year ending on 31st March 1997:

(*a*) Salary Rs. 1,500 p.m.
(*b*) Bonus at two months' salary
(*c*) Commission equal to four month's salary
(*d*) Entertainment allowance at Rs. 500 p.m.
(*e*) Conveyance allowance at Rs. 400 p.m.
(*f*) He was provided with free furnished quarter valued at Rs. 600 p.m. for rent and Rs. 200 p.m. for furniture and fittings
(*g*) He was provided with free lunch at the Corporation valued at Rs. 6 per day for 300 working days. He was employed in this Corporation since April 1957.
(*h*) He contributed to the Corporation's Recognised Provident Fund @ Rs. 500 p.m., the Corporation contributing an equal amount. Interest credited to this fund at 12% p.a. was Rs. 3,600.
(*i*) He received Rs. 16,000 as Net Dividends from various Indian companies.
(*j*) He paid during the year:
  (*i*) Rs. 6,000 as premium on his own life policy for Rs. 50,000.
  (*ii*) Rs. 5,000 as premium on his joint life policy with his wife.
  (*iii*) Rs. 8,000 in 15-year Cumulative Time Deposit A/c in the Post Office.
(*k*) He claims deductions for:
  (*i*) Car maintenance expenses and its depreciation at Rs. 900 p.m. Car is used equally for employment and personal purposes.
  (*ii*) Cost of books and periodicals necessary for his duties was Rs. 1,000.
  (*iii*) Entertainment and conveyance allowances in full.
  (*iv*) Electricity and water charges incurred by him for his residence Rs. 1,000 per annum. Compute his Total Income.

[Hints: Value of house 5,700; Salary Income 28,600; Other sources 20,000; G.T.I. 48,600; Deduction u/s 80L 15,000; Total Income 33,600; Q.A. for rebate of tax u/s 88 Rs. 25,000 Tax NIL] [P-17]

Q. No. 10

Mr. X started construction of 3 equal and independent units of House property on 1.4.95 and completed them on 28.3.96. These were let out from 1.4.96. The particulars are given below :

Nature of occupation	I Self occupied	II Letout for residence	III Used for own business
	Rs.	Rs.	Rs.
Actual Rent received	NIL	84,000 p.a.	NIL
Fair Rental Value	72,000	72,000	72,000
Municipal Taxes			
(*a*) paid by owner	7,200 p.a.	4,200 p.a.	9,000 p.a.
(*b*) paid by tenent		4,200 p.a.	
Ground Rent (due)	3,000 p.a.	3,000 p.a.	3,000 p.a.
Land Revenue (due)	3,600 p.a.	4,200 p.a.	4,500 p.a.

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For construction of these units he took a loan of Rs. 10,00,000 on 1.4.95. Rate of interest is 12%. The total cost of construction of all these units is Rs. 24,00,000. His business profit without debiting the expenses of unit III is Rs. 1,80,500. Compute his total income in relation to assessment year 1997-98.

(C.A. Inter Nov. 93 Adapted)

[**Hints :** Self occupied House Loss ~~10,000~~ 15,000; Letout house Income Rs. 20,840; Business Income Rs. 44,000; Total Income Rs. 54,840, Tax Rs. 2,968] [P-2]

Q. No. 11

Mr. P.K. Nair is an employee getting salary of Rs. 5,000 p.m. He occupies a house for his residential purposes at Delhi, whose rent is Rs. 1,500 p.m. Mr. Nair does not own any house on his own name or on the name of any member of his family. Compute total income of Mr. Nair in the three different situations given below:

(*a*) The employer is the tenant and pays the rent to landlord direct.

(*b*) The employer gives Rs. 1,200 p.m. as house rent allowance to Mr. Nair and rent is paid to landlord by Mr. Nair.

(*c*) Mr. Nair pays the rent but does not get anything from his employer.

[**Hints:** (*a*) To be treated as rent-free house value Rs. 6,000. Total Income 51,000; (*b*) To be treated as House rent allowance HRA exempted u/s 10 (13A) 12,000, Total Income 47,400; (*c*) Eligible for deduction u/s 80 GG; Gross Total Income Rs. 42,000; Deduction u/s 80GG 10,500; Total Income 31,500] [P-26]

Q. No. 12

Shri Sunil Khandelwal, branch manager of the Hindustan Lever Ltd., Delhi has furnished the following details with regard to his income for the year ended on 31st March, 1997:—

(*a*) (*i*) Salary @ Rs. 2,000 p.m.
(*ii*) Bonus Rs. 12,000
(*iii*) Conveyance Allowance @ Rs. 500 p.m.
(*iv*) Entertainment allowance @ Rs. 250 p.m.
(*v*) Provided with an unfurnished house by the employer at Rs. 200 p.m. for which the company is paying a monthly rent of Rs. 2,175.
(*vi*) Personal medical bills reimbursed by the employer, Rs. 4,000.
(*vii*) His contribution to Company's unrecognised provident fund is @ Rs. 400 per month. The employer contributes an equal amount. The interest credited to the Provident Fund A/c at 10% per annum is Rs. 4,000.
(*viii*) He is employed with this company since 1st April, 1960.

(*b*) Interest on Government Securities (Gross) Rs. 4,000.

(*c*) (*i*) Sold on 1st April, 1996 [C.I.I. = 305] one house for Rs. 1,24,400. This house was purchased by him on 1st April, 1971 for Rs. 25,000. The market value of this house on 1st April, 1981 [C.I.I. = 100] was Rs. 40,000.
(*ii*) Sold another house also on 1st April, 1996 for Rs. 50,000. This house was purchased by him on 1-6-1994 for Rs. 38,000.

(*d*) Income from units of the Unit Trust of India, Rs. 3,000.

(*e*) Life Insurance premium paid during the year Rs. 4,000.

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(*f*) Donation to Prime Minister's National Relief Fund Rs. 2,000.

(*g*) Donation to the Government to be utilised for the promotion of family planning Rs. 2,500.

Work out his Total Income for the assessment year 1997-98.

(B.Com. Punjab 1986)

[**Hints**: Salary Income 31,400 (conveyance allowance fully taxable, Value of House 2,100); Capital gain 14,400. G.T.I. 52,800; Deduction u/s 80L 7,000; 80G: 4,500; Total Income 41,300 Q.A. for rebate of tax u/s 88 Rs. 4,000] [Tax Rs. 260 Rebate u/s 88 Not allowed] [P-7]

Q. No. 13

Following are the particulars of incomes and expenses of Shri Mayank Agarwal for the year ended 31st March 1997.

(*a*) He is an employee of *Life Insurance Corporation of India* posted at Delhi. He is drawing a basic Salary of Rs. 5,000 p.m. He gets dearness allowance @ Rs. 1200 p.m. of which 1/2 is treated as Salary for computation of retirement benefits. He has been provided with the facility of a 12 horse power car with a driver, the running and maintenance expenses whereof are met by the employer. The car is used by him both for the official and personal purpose. The employer has also provided him a rent-free furnished house, the fair rental value whereof is Rs. 2,000 p.m. and the charges paid by the employer for the furniture, air conditioner, etc. amounted to Rs. 3,000 a year.

(*b*) He contributes to a provident fund @ 10% of his salary and the employer contributes 12% of salary.

(*c*) He paid Rs. 4,000 as insurance premium on a joint life policy on his and wife's life. He had also purchased National Savings Certificates (VIII issue) of the value of Rs. 10,000.

(*d*) He received Rs. 4,000 as dividend from an Indian Company and Rs. 4,500 as interest on debentures of a company. Both such shares and debentures are listed in Delhi Stock Exchange.

(*e*) He is a partner in a firm assessed as AOP alongwith his wife and each of them received an amount of Rs. 5,000 being their 1/10th share of profit.

(*f*) He received an amount of Rs. 8,000 from betting in a club.

(*g*) He Paid Rs. 30 as collection charges to his bank for the collection of interest.

Compute his total income for the assessment year 1997-98

(B.Com. Punjab, 1987)

[**Hints :** Salary income Rs. 79,920; P & G Rs. 5,000; Other sources Rs. 12,970; Deduction u/s 80L Rs. 5,000; Total Income Rs. 92,890; Tax Rs. 13,167 Rebate of Tax u/s 86 not allowed and u/s 88 Rs. 4,144. Net Tax Rs. 9,023 No clubbing of wife's share from AOP] [P-12]

Q. No. 14

A musician and a playback singer, entrusts his accounts to you for preparation of a return of income for the assessment year 1997-98. Compute tax liability also.

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Form an analysis of the Bank accounts, you notice the following:

		Rs.
(*i*)	Programme receipts (local)	24,000
(*ii*)	Receipts from film producers and companies	68,000
(*iii*)	Royalty receipts from companies on records sold	20,000
(*iv*)	Amount from Life Insurance Corporation on maturity of a policy in the name of his wife	46,000
(*v*)	Interest on Savings Banks accounts	1,650
(*vi*)	Interest on Fixed Deposits with Banks	8,500
(*vii*)	Life Insurance premium paid on a policy in wife's name (Sum assured Rs. 2 lakhs)	22,500
(*viii*)	Life Insurance premium paid on a policy on his own name (Sum assured Rs. 1,00,000)	8,000
(*ix*)	Deposited in a public providend fund account	40,000
(*x*)	Cost of train and air tickets for a party taken by A, on a concert tour of Calcutta, Shillong and Guwahati	14,000
(*xi*)	Payments to accompanying artists for the above	8,000
(*xii*)	Concert receipts of the tour of Eastern India region	65,000
(*xiii*)	Motor car expenses—car used to attend concerts, recording sessions etc.	14,000
(*xiv*)	Rent paid (half the premises used for professional purposes)	9,000

X also trains disciples in his spare time and in the relevant year, he collected from such disciples Rs. 12,000 in cash which were utilised to meet the household expenses. X has some agricultural lands in his ancestral village and in the year, he received Rs. 4,000 by way of sale of paddy. His father had left him some government securities, on which he collected interest (gross) of Rs. 1,200 in the year.

Compute A's total income. *[Adapted C.A. (Inter) 1987]*

[**Hints:** Professional Gain inclusive of royalties Rs. 1,48,500; Income from other sources Rs. 11,350; Deduction u/s 80L 11,350; Total Income Rs. 1,48,500. Integration of Agri. income with this total income for tax purposes Q.A. for rebate of tax u/s 88 Rs. 70,000 Rebate @ 25%Net tax payable Rs. 15,900] [P-20]

Q. No. 15

Shri Mukul Jain, a resident of Bombay, submits the following details of income for the financial year 1996-97:

1. Salary Rs. 2,800 p.m.
2. D.A. Rs. 300 p.m.
3. Entertainment Allowance Rs. 300 p.m. (Prior to 1-4-55 he was getting Rs. 200 p.m.)
4. City Compensatory Allowance Rs. 100 p.m.
5. Bonus Rs. 3,000.
6. Employer's contribution to the Recognised. P.F. Rs. 4,000.
7. His own contribution to R.P.F. is also Rs. 4,000.
8. Interest on the accumulated balance of the Fund @ 10% p.a. Rs. 14,000.

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9. He is provided with an unfurnished house for which the employer charges Rs. 200 p.m., the municipal value of the house being Rs. 6,000 p.a.
10. He is also provided with a chauffeur driven 20 H.P. car by the employer. The Car is used for official and private purposes both and the entire expenses of its running and maintenance are met by employer.
11. During the year Mr. Jain has received dividends from an Indian Co. amounting to Rs. 6,400 (Net).
12. He contributed Rs. 2,000 in U.L.I.P. and purchased N.S.C.'s (VIII issue) worth Rs. 6,000 in the previous year. The interest accrued on N.S.C.'s (VIII issue) purchased in an earlier year amounted to Rs. 2,400. He donated Rs. 2,000 towards Prime Minister's National Relief Fund. Compute his taxable income for the assessment year 1997-98. *(P.U. B.Com., April, 1989)*

[**Hints**: Value of Rent free house Rs. 1,500; Standard deductions Rs. 18,000 as his salary income does not exceed Rs. 60,000 (60,340 – 2,400); Salary Income Rs. 39,940; Other sources Rs. 10,400; Deduction u/s 80 G Rs. 2,000; 80L Rs. 10,400 Total Income Rs. 37,940; Q.A. for rebate u/s 88 Rs. 14,400] [P-10]

Q. No. 16

From the following particulars, calculate the taxable income and rebate available under Section 88 for assessment year 1997-98 :

	Rs.
Salary per month	6,000
Dearness allowance per month	600
House rent allowance per month	1,000
(Rent paid Rs. 1,500 p.m.)	

House property is let out on a monthly rent of Rs. 2,000. The annual value of the house property is Rs. 30,000. Municipal tax paid is Rs. 1,800 for whole year. Interest payable on capaital borrowed for the construction of the house is Rs. 6,000. Repayment of house building loans taken from friends is Rs. 5,000 and from Life Insurance Corporation is Rs. 3,000.

	Rs.
Interest on Savings Bank A/c	4,000
Dividend on master shares of UTI	3,000
Interest on PPF A/c	2,000
Income from units of Unit Trust of India	4,000
Life insurance pemium	6,000
Contribution to public provident fund	6,000
Deposits in account under National Saving Scheme (1992)	10,000
Interest accrued on NSC's VIII issue	4,000

The construction of the building was completed on 1st January, 1992.
(C.A. Inter Nov. 1992)

[**Hints** : Salary Income Rs. 65,400, House Property Rs. 14,400, Other Sources Rs. 15,000, Deduction u/s 80L Rs. 15,000, Total Income Rs. 79,800, Q.A. for rebate u/s 88 Rs. 29,000] [P-13]

Q. No. 17

From the following details compute the total income of Mr. X, a resident of Delhi, amount of tax and rebate available for the assessment year 1997-98 :

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	Rs.
(*a*) Salary including dearness allowance	66,000
Bonus	9,600
Contribution to a recognised provident fund	6,000
Life Insurance Premium	15,000
Rent paid by the employer for flat provided to Mr. X	48,600
Cost of furniture provided by the employer at the aforesaid flat	40,000
Rent recovered from Mr. X by employer	12,000
Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	3,000

Mr. X was provided with company's car (self driven) also for personal use ; not possible to determine expenditure on personal use and all expenses were borne by the employer.

(*b*) Mr. X owns a house	
Rent received (12 months)	36,000
Municipal valuation	24,000
Municipal taxes paid	6,000
Ground rent	1,400
Insurance charges	560
Collection Charges	1,700
Interest on borrowing used for construction of house. The house was constructed on 30.6.1991	25,700
(*c*) Dividend received from Unit Trust of India	7,000
Deposits under National Savings Scheme (1992)	10,000

(*d*) A house was purchased by Mr. X on 1.5.1985 for Rs. 2,00,000 and was used as a residence by the owner.

The owner had contracted to sell this property in June, 1990 for Rs. 8 lakhs and had received an advance of Rs. 50,000 towards sale. The intending purchaser did not proceed with the transaction and the advance was forfeited by the owner.

The property was sold in July, 1996 for Rs. 10,00,000. The owner, from out of the sale proceeds, invested Rs. 3 lakhs in a new residence in December, 1995. [C.I.I for 1985-86 is 133 and for 1996-97 is 305]

[*C.A. Inter May 1993 (Adapted)*]

[Hints : Value of rent free House Rs. 2,800 ; Salary income Rs. 73,600; House Property loss Rs. 4,380 to be set off; L.T.C.G. [6,56,015 – Exemption u/s 54 Rs. 3,00,000] 3,56,015; Other Sources Rs. 7,000, Deduction u/s 80L Rs. 7,000, Total Income Rs. 4,25,235, Q.A. for rebate u/s 88 Rs. 31,000 Tax : (LTCG 71,203 + 5,766 less rebate u/s 88 5,766 = Rs. 71,203] [P-14]

Q. No. 18

Shri Jankidas is an employee of a tea plantation in Assam and furnishes you with the following information to enable you to compute his total income for the previous year ended 31st March, 1997.

(*a*) Basic salary—Rs. 5,000 per month.

(*b*) Dearness allowance—40% of basic salary according to the terms of employment.

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(*c*) Children's education allowance—Rs. 500 per month.

(*d*) Bonus—30% of basic salary.

(*e*) Entertainment allowance—Rs. 1000 per month, Mr. Jankidas has been with the company from 1953 since when he has been receiving the allowance.

(*f*) Recognised provident fund—own contributions @ 10% of salary and D.A., Company's contribution @ $12^1/_2$ of salary and D.A.

(*g*) Employee's contribution to approved super-annuation fund $7^1/_2$% of basic salary.

(*h*) Interest on accumulated balance of provident fund at 10% p.a.—Rs. 4,000.

(*i*) Shri Jankidas received an amount of Rs. 50,000 by way of compensation from Oriental Assurance Company for motor accident in which he had got injured about two years ago. The Court also awarded a sum of Rs. 5,000 by way of interest for delayed payment of compensation.

(*j*) Shri Jankidas owns a car which he uses both for official and personal purposes, the expenses being met by Company. During the year these expenses amounted to Rs. 8,400. It is estimated that 20% of the expenses are for personal use.

(*k*) Shri Jankidas is provided with rent free accommodation (furnished) within the plantation area, the fair rent of which is Rs. 900 p.m. He is not eligible to the accommodation during the annual vacations for two months. The original cost of the furniture available in the house is Rs. 40,000.

(*l*) He was paid a sum of Rs. 10,000 by his employer as he saved the company from heavy damage.

(*m*) He received dividend from Indian Companies of Rs. 5,000 gross.

[**Hints :** Value of rent free house Rs. 12,333; salary income Rs. 1,22,413; Other Sources Rs. 10,000; Total Income Rs. 1,27,413; Tax payable Rs. 23,964 Less rebate u/s 88 Rs. 2,580 = 21,384; Compensation fully exempted; Interest on delayed payment taxable under Other Sources] [P-16]

Q. No. 19

Following particulars are furnished by X, an Idnian citizen, for the year ending March, 31, 1997:

	Rs.
Salary (Net of tax and X's contribution to recognised provident fund)	48,000
X's contribution to provident fund	4,200
Employer's contribution to provident fund	4,200
Interest credited to provident fund @ 8.75 per cent per annum	14,000
Travelling expenses for proceeding on leave to home town	3,600
House rent allowance (rent paid: Rs. 4,500)	4,500
Dividends from PQR Ltd., an Indian company (net of tax)	2,500
Dividend collection charge	200
Winning from lotteries (net of tax)	9,000
Colletion charges of lottery prize	150

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Winning from horse races (net of tax)	6,000
Tax deductin at source on :	
—salary	1,500
—dividend	NIL
—winning from lotteries	6,000
—winning from horse races	4,000
Contribution to public providend fund	4,000

Determine the total income of X and tax payable for the assessment year 1996-97.

[Company Secretary Inter June, 1993]

[**Hints :** Salary [Rs. 48,000 + 1,500 + 4,200] Rs. 53,700; HRA Fully Taxable, salary income Rs. 40,200, other sources Rs. 22,300 Deduction u/s 80L Rs. 2,300 Total Income Rs. 60,200 Tax Rs. 8,030, Less rebate u/s 88 Rs. 1,640, Less T.D.S. Rs. 11,500 Refund due Rs. 5,110] [P-19]

Q. No. 20

X a resident individual retired from AB Co. Ltd., on 1st February, 1997 after 20 years and 9 months of service. He joined PZ Co. Ltd., on the same day, *i.e.* 1st February, 1997 and remained in service till 31st March, 1997 when he furnished the following information :

Salary and allowances from 1.4.1996 to 31.1.1997 from AB Co. Ltd.: (Due on last day of month)

	Rs.
Basic Salary	8,000 p.m.
Dearness allowance	1,000 p.m.
Commission calculated @ 4% on turnover of Rs. 1,00,000 achieved by X	4,000
Gratuity received (not covered by the payment of Gratuity Act, 1972)	1,05,000

Salary and allowances from PQ Co. Ltd. (Due on last day of month]

	Rs.
Basic Salary	6,000 p.m.
Entertainment allowance	800 p.m.
Fixed medical allowance	200 p.m.
House rent allowance	500 p.m.
Leave salary received	3,000

Other informations :

X resides in his own house throughout the year, on which municipal tax of Rs. 5,000 has been paid during the year.

X is also the partner of XYZ Co., a partnership firm assessed as a firm as such and receives a share income of Rs. 11,140 from the firm during the previous year ended on 31st March, 1997 (it does not include remuneration and interest). He incurs a loss of Rs. 4,820 from a speculation business carried on during the year.

X received Rs. 2,500 as interest on Post Office Saving Bank Account and Rs. 1,500 as dividend from a company incorporated in England. Interest on deposits in companies in the name of his minor son amounted to Rs. 4,000.

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X paid a premium of Rs. 10,000 on the policy of Rs. 70,000 on life of his minor child. Contribution to an approved superannuation fund and the Jeevan Dhara Scheme of the LIC amounted to Rs. 7,500 and Rs. 4,500 respectively.

Compute X's total, income tax and tax rebate available under section 88 of the Income-tax Act, 1961, for the assessment year 1997-98.

[C.A. Inter Nov. 1995]

[Hints : Taxable gratuity Rs. 21,000; Salary Income Rs. 1,18,000; Speculation loss to be C/F; share of income from PFAF is exempted; other sources Rs. 1,500 + (4,000 – 1,500); Total Income Rs. 1,22,000; Tax liability Rs. 21,800 less rebate of tax u/s 88 Rs. 4,400] [P-18]

Q. No. 21

Lakshmi is employed in Delhi. She submits the following particualrs of his income and payments for the assessment year 1997-98 :—

Income/Receipts	Rs.
Basic salary	90,000
Dearness allowance [Enters into pay for service benefits]	20,000
House rent allowance	12,000
City compensatory allowance	1,200
Medical allowance	4,800
Examinership fee received from another institution	5,000
Interest from bank on fixed deposit in the name of husband [Amount gifted by her]	15,000
Dividend from Unit Trust of India	3,000
Birthday gift	5,000
Payments	
Contribution to general providend fund and life insurance premium	17,000
Repayment of providend Fund loan	12,000
Refund of house building loan	12,000
Rent actually paid in Delhi	24,000
Investment in SBI Magnum Tax Saving Scheme under section 88	10,000
Deposits under the National Saving Scheme 1992	20,000

Determine taxable income and tax for the assessment year 1997-98.

[Company Secretary Inter Dec. 1990]

[Hints : Salary Income Rs. 1,01,000; Income from other sources Rs. 23,000; Total Income Rs. 1,09,000; Deduction u/s 80L Rs. 15,000; Tax liability Rs. 17,700 Less rebate u/s 88 Rs. 11,400] [P-21]

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2 ASSESSMENT OF HINDU UNDIVIDED FAMILY

Schools of Hindu law— Residence of H.U.F.— Assessment of H.U.F.—Rebate u/s 88—Partition of H.U.F.—Impartible Estate—Income not to be treated as family income— Illustrations and Questions.

The Income-tax Act provides for a special status to a Hindu Undivided Family and it is assessed to income-tax as a separate unit of assessment. The act has not defined the concept of Hindu undivided family. For this purpose we have to depend upon Hindu law.

Generally speaking, the concept of Hindu Undivided Family means a group of persons lineally descendent from a common ancestor and includes their wives and unmarried daughters. It comes into existence due to a certain relationship and it cannot come into existence by an agreement among strangers.

To claim the status of Hindu Undivided Family, a family must satisfy the following two conditions:

1. *Existence of common property in the family.* The common property may consist of ancestral property inherited from a male ancestor, property acquired with the aid of ancestral property and property acquired by an individual from his own sources but put into common pool of Hindu Undivided Family.

2. *Existence of Hindu Coparcenary.* When there is a person who can claim share in the property of Hindu Undivided Family on partition, he is known as Coparcencer.

Schools of Hindu Law

Mitakshara School. Under this school of law the male child acquires a right in the family property as soon as he is born in the family. As soon as a male child is born, the Hindu Undivided Family comes into existence. The father gets the status of 'Karta'— the manager of the family. On the death of father this status goes to eldest son in the family till partition of the property takes place. In this school of law, share of each member is not defined. No member can ask what his share is.

Dayabhaga School. Under this school of law the male child does not acquire a right in the family property during the life time of his father. During the life time of the father, the income from ancestral property is included in his individual income. On the death of father, the coparcencer gets his definite share. Coparcenary comes

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into existence only on the death of the father if there are two coparceners at the time of death. In this school of law, even the females can become the members of the undivided family.

The coparcenary will come into existence even if there are female members, *i.e.*, widow and an unmarried daughter to succeed him. But if the father leaves only a son behind him, the son cannot form a coparcenary and he will be taxable as individual.

On the death of father, if there are four sons and before the partition takes place, two of them die leaving behind widows; in this case the widows shall become coparceners and shall be taxable as Hindu Undivided Family.

Under this school of law, the concept of Hindu undivided Family comes into existence only on the death of father and remains into existence only up to the time of partition of common property.

A husband and wife without any children can form a Hindu Undivided Family and there is no need for more than one male coparcencer to form H.U.F. *[Gowli Buddanna v. C.I.T. (60 ITR 293)]*.

Residence of H.U.F.

Section 6(2) of the Act provided that a Hindu Undivided Family shall be resident in India in a previous year in all cases except when control and management of its affairs is wholly situated outside India. In other words, if even a small part of control or management is situated in India it will be a resident Hindu Undivided Family.

Non-Resident. If the control and management of the affairs of a Hindu Undivided Family is situated wholly outside India it is non-resident Hindu Undivided Family.

Not Ordinary Resident. A Hindu Undivided Family can claim the status of 'Not Ordinarily Resident' if the 'Karta' (Manager) of H.U.F. can prove that:

(*a*) He was not a resident of India for 9 out of 10 previous years preceding the relevant previous year, or

(*b*) He was not in India for a period totalling 730 days or more during 7 previous years preceding the relevant previous year.

Assessment of Hindu Undivided Family

The Hindu Undivided Family is a separate unit of assessment and is taxable through its manager or Karta. A single person, male or female, does not constitute a family. The following *rules* are to be observed while making the assessment of Hindu Undivided Family:

1. Once a family is accorded the status of Hindu Undivided Family, it shall continue to enjoy this status till partition takes place and I.T.O. accepts the partition u/s 171.

2. The share of income received by a member of H.U.F. from the income of family is not to be included in his individual income being exempted in the hands of the coparcencer of H.U.F. even though the family may not have paid the tax on such income.

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3. The income received by a member from an asset which was previously owned by him but has been put into common pool of H.U.F. shall remain as his individual income.

4. Salary paid out of the fund of H.U.F. to a member is allowed as the legitimate expenditure of the H.U.F., if the member has rendered some service to the H.U.F. *[Jugul Kishore Baldeo Sahai v. C.I.T. (U.P) Supreme Court 1966].*

5. A member can carry on any business in his own name and the income from such business shall be included in his individual total income. It is immaterial that the funds were provided by H.U.F.

6. Jain and Sikh families are also treated as Hindu Undivided Families.

7. A gift of property to the wife out of the family property is a bonafide transfer and as such income from such property shall belong to the wife.

8. On the death of manager, the succeeding manager— not the member of family or wife, shall be his legal representative.

9. In case any H.U.F. holds shares in a company and any loan is advanced to members of H.U.F., it will not be deemed as dividend u/s 2 (22) (e) because individual members are not shareholders of that company. *[Rameshwarlal Sanwarmal v. C.I.T. Assam].*

Rebate of tax u/s 88

Hindu Undivided Family is also entitled to claim rebate of tax on long term approved savings. Rebate of tax is allowed on Qualifying amount as calculated below:

Qualifying Amount

(*i*) *Contribution made by H.U.F.* in Public Provident Fund on the name of any of its members fully qualifies.

(*ii*) Life Insurance Premia—Premium paid by H.U.F. to get the insurance policy on the life of any member of H.U.F. shall qualify upto actual premium paid.

(*iii*) Any amount paid by H.U.F. as repayment of loan taken to purchase or construct the house or payment of price of house purchased from Govt. or Govt. agency shall qualify upto actual amount repaid or Rs. 10,000 w.e. is less.

(*iv*) Any amount deposited in 10 year or 15 year C.T.D account fully qualifies.

(*v*) Any amount deposited under a deposit scheme of National Housing Bank shall also fully qualify.

(*vi*) Any amount spent to purchase National Savings Certificates VIII issue on the name of any member of H.U.F. shall also fully qualify. Any interest accruing on VII issue shall become eligible for deduction in the succeeding previous years.

Limit on Qualifying Amount

The sum total of all the above-mentioned savings (*i*) to (*vi*) cannot exceed Rs. 60,000 in a previous year. It can be expressed as—Actual total savings made in the previous year or Rs. 60,000 whichever is less is qualifying amount.

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Rate of Rebate. H.U.F. will be entitled to claim rebate of tax @ 20% of qualifying amount subject to a maximum of Rs. 12,000 in a year. H.U.F. is **not** entitled to additional relief of Rs. 2,000 for investment in notified bonds share or units.

Partition of Hindu Undivided Family (Section 171)

Total Partition. It means a physical partition of the property of the family, *i.e.* where property admits of a physical division. But mere division of the income from the family property without division of property shall not be considered as a partition.

In case property does not admit the physical division, such division as the property admits or mere severing of relationship shall not be considered as partition.

If a joint family has come to an end, in fact and in law but no physical division of the property has taken place, the family will be deemed to continue as Hindu Undivided Family.

Partial Partition. Where the joint family continues but only some properties are partitioned by physical division and other continue to be owned by Hindu undivided family. H.U.F. shall be assessable for the income of the properties still owned by it.

There Finance Act (2) 1980 has amended section 171 of the Act to provide for banning of partial partition of the property of Hindu Undivided Family as a measure to check tax evasion. With effect from 31-12-78, any partition of the property of the H.U.F. shall be deemed to have not taken place and no benefit under income-tax Act shall be available on account of such partition.

Assessment on Partition

In case I.T.O. is satisfied that the partition has taken place during the previous year and records his findings to this effect, in such an event the total income to the H.U.F. up to the date of partition shall be assessed in the hands of H.U.F. as if no partition has taken place. Each member of the family shall be liable jointly and severally for the tax liability of H.U.F.

Impartible Estate. In certain cases a person holds some property which is family property but is still not divisible among other members. The income from such property belongs absolutely to the person who holds it. The income from such property shall not be included in the total income of H.U.F. It will be included in the total income of individual who holds property.

Income not treated as family income

1. Income earned by a member of H.U.F. in his individual capacity with his own efforts shall be his individual income.
2. Income of the father from property other than ancestral inherited property, shall be his individual income and not the income of H.U.F.
3. Income from impartible estate shall be the income of individual who holds it.
4. Income from a business carried on by a member of H.U.F. in his individual capacity is assessable in his hands. It is immaterial whether the capital for business was provided by the family.

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5. Income received by a member of H.U.F. for acting as director of company in his individual capacity and when he is not representing H.U.F. is individual income.

6. On the death of father if there is sole surviving male member he will not constitute H.U.F. Instead he will be assessable as individual.

7. Income of a member received by way of profits from firm in which he is partner in his individual capacity shall be his own income.

Individual Income or Family Income

In case Karta of H.U.F derives some salary, commission etc. from company, firm etc. in which the funds of the family were invested, such remuneration received shall be taxed in the hands of the H.U.F. and not in the individual capacity of the Karta. It is contented in this case that the income is primarily earned by investing family funds on assets and the amount of personal efforts or services rendered by the Karta shall not alter character of the income. A similar view was expressed by the Supreme Court in the case of *P.N. Krishana Iyer v. C.I.T. (1969) 73 I.T.R 539.* However, in case the circumstances of the case state that the remuneration received was for services rendered by him and there was no real and sufficient connection between the investment of family funds and the remuneration paid to manager, the remuneration received by the Karta shall be assessed as individual income of Karta and not that of the H.U.F. The Supreme Court also held the similar view is the case of *Prem Nath and others v. C.I.T. (1970) 78 I.T.R. 319 S.C.)*

Illustration 1. K, the manager of a H.U.F. was admitted to partnership to represent family. Under the terms of partnership deed K was entitled to the salary of Rs. 1,000 p.m. for rendering service to the firm. Decide whether salary received by Mr. K is his individual income or the income of H.U.F.

Solution

Mr. K was representing that family in the firm. As such the profits received by him from the firm shall constitute the income of the H.U.F. but the salary received by him for services rendered to firm, is the compensation for his individual effort and as such shall remain to be his individual income. The salary, therefore, cannot be treated as family's income.

[Prem Nath and others v. C.I.T. (1970) 78 I.T.R. 319 (S.C.)]

Illustration 2. The following details of income have been supplied by Karta of H.U.F. You are required to compute the total income and tax of H.U.F. The family has no member whose independent income exceeds Rs. 40,000. It has deposited Rs. 10,000 in PPF:

		Rs.
(*i*)	Profit from business	32,000
(*ii*)	Salary received by a member of H.U.F.	8,000
(*iii*)	Director's fee received by Karta	6,000
(*iv*)	Rental value of the property let	12,000
(*v*)	Municipal Taxes	600
(*vi*)	Dividends	450

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(*vii*) Long-term Capital gains from the transfer of building 9,500
(*viii*) Long-term Capital gains from the transfer of investments 10,000
(*ix*) Donation to a college which is an approved institution 4,000
(*x*) Profit from a firm assessed as AOP (1/4th share) 10,000

(B.Com. Punjab, Modified)

Solution

Computation of Total Income of H.U.F.

	Rs.	Rs.
Income from House Property:		
Annual Rental Value	12,000	
Municipal Taxes	600	
Annual Value	11,400	
Deduction:		
1/5th of Net A.V. for repairs	2,280	
		9,120
Income from Business:		
Business Profit	32,000	
$^1/_4$th Share from firm assessed as AOP	10,000	
		42,000
Capital Gains:		
Long-term Capital Gains from Building	9,500	
Long-term Capital Gains from Investments	10,000	
		19,500
Income from other Sources:		
Dividend		450
Gross Total Income		71,070
Deductions:		
U/s 80 L: Dividend	450	
U/S 80 G: Donations Q. A. Rs. 4,000	2,000	
(within 10% of G. Taxable. I.) Rate 50%		2,450
Total Income		68,620

Computation of Tax (ordinary H.U.F.)

On L.T.C. Gain of Rs. 19,500 20%	3,900
On balance total income [68,620 – 19,500 = 49,120]	
Rs. 40,000 of Total Income	NIL
Balance Rs. 9,120 @ 15%	1,368
	5,268
Rebate of Tax : Q.A. Rs. 10,000 @ 20%	
Rs. 2,000 but restricted to tax on regular income *i.e.*	1,368
Net Tax Payable	3,900

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Notes: 1. Salary received by a member is his individual income.

2. Director's fees received by Karta is presumed to be his individual income.

3. No rebate u/s 86 on share from AOP as AOP's income does not exceed Rs. 40,000.

Illustration 3. X is the Karta of a Hindu Undivided Family, Y and Z are his two major sons. From the following particulars, compute the total income and tax of H.U.F.

(*i*) The H.U.F. runs a business in cotton textiles. The net profit of the business was Rs. 21,000 after charging Rs. 11,000 paid as salary to Y and Z for their help in running the business.

(*ii*) Profit and Loss Account shows an entry of drawing of Rs. 20,000.

(*iii*) The assessee has failed to furnish satisfactory explanation regarding a deposit of Rs. 20,000 in the name of X.

(*iv*) Remuneration received by Karta for acting as Director of a company in which H.U.F. holds shares worth Rs. 2 Lakhs: 10,000.

(*v*) Dividend received by H.U.F. Rs. 6,944, Tax deducted at source Rs. 1,736.

(*vi*) Sale proceeds of a shop acquired in 1978, sold on 31-12-96 for Rs. 81,250. Fair market value on 1-4-81 estimated to be Rs. 25,000. [C.I.I. for 1981-82 is 100 and for 1996-97 is 305]

(*vii*) H.U.F. has paid Rs. 12,000 as premium on the Life Insurance Policies of Y & Z for Rs. 1,00,000.

(*viii*) One of his major sons is working as Manager in a private Limited Company and is getting a salary of Rs. 60,000 p.a.

(*ix*) Deposited Rs. 2,000 in PPF on the name of Z.

Solution

Computation of Total Income of H.U.F.

		Rs.	Rs.
Income from Business			
Net profit as per Profit and Loss Account		21,000	
Add: Drawings		20,000	
			41,000
Income from Capital Gains			
Sale price of Shop		81,250	
Fair Market Value as on 1-4-81 Rs. 25,000 (Indexed 25,000 × 305/100)		76,250	5,000
Other Sources			
Cash credit (for which no satisfactory explanation has been provided by assessee) u/s 68		20,000	
Remuneration received by Karta for acting as Director		10,000	
Dividend (Net)	6,944		
Tax Deducted at source	1,736		
		8,680	
			38,680

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Gross Total Income		84,680
Deduction u/s 80L: Dividend		8,680
Total Income		76,000

Computation of tax

On L.T.C. Gain of Rs. 5,000 20%		1,000
On Balance Total income [Rs. 76,000 – 5,000 = Rs. 71,000]		
On Rs. 60,000	3,000	
On Balance Rs. 11,000 @ 30%	3,300	6,300
		7,300
Rebate of tax u/s 88 Q.A. Rs. 14,000 @ 20%		2,800
Net Tax		4,500

Notes: 1. Salaries given to the members of H.U.F. is allowed as business expenditure of the H.U.F.
2. He is presumed to be the Director because of shares held by family.
3. Q.A. for Rebate of Tax u/s 88: L.I.P. Rs. 12,000+P.P.F. Rs. 2,000 = Rs. 14,000.

Illustration 4. Mr. Sohan, an individual converted his self-acquired property amounting Rs. 60,000 into H.U.F. property on 1-6-83. The H.U.F. consists of himself, his wife, a major son and a minor son. The H.U.F. earned an income of Rs. 1,00,000 from other sources. The income from the property converted into H.U.F property is Rs. 12,000 and his wife and minor son are entitled to a share in it. Compute the total income of H.U.F. and total income of Mr. Sohan if Mr. Sohan has Rs. 15,000 as his individual income.

Solution

Computation of Total Income of H.U.F.

		Rs.
1.	Income from all other sources	1,00,000
	Gross Total Income being Total Income	1,00,000

Computation of total income of Mr. Sohan :

		Rs.	
I.	Income from all other sources	15,000	
II.	Share of income from the property converted into H.U.F. Property [u/s 64(2)]	12,000	
	Total Income		27,000

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Q. No. 1

The following particulars have been submitted by Mr. Ram Lal in the capacity of Karta of a Hindu undivided family for assessment purposes:

(*a*) Profit from family's business, Rs. 20,000 after charging an amount of Rs. 3,000 given as salary to Karta's brother who has been actively participating in it.

(*b*) Salary income of Karta's another brother who is a manager in a Cooperative Bank, Rs. 11,000.

(*c*) Director's fees received by Karta, Rs. 5,000.

(*d*) Dividend Rs. 400 (Gross).

(*e*) Long-term capital gain from the transfer of building, Rs. 2,800.

(*f*) Long-term capital gain from the transfer of investments Rs. 18,000.

(*g*) Donation to a college which is an approved institution, Rs. 6,000.

(*h*) Rental value of the property let, Rs. 15,000, municipal tax paid in respect of the house, Rs. 1,500. Interest on loan taken for repair of house is Rs. 1,800.

You are required to calculate total income of the family for the current assessment year. *(B.Com., Guru Nanak)*

[**Hints.** House Property Income 9,000, Business Income 30,000, Long Term Capital Gain 10,800, other sources 5,400 (it is assumed that Karta is director because of shares held by H.U.F.) G.T.I. 55,200. Deduction u/s 80G: 1,700, 80L: 400; Total Income Rs. 53,100]. [P-5]

Q. No. 2

Mr. Ramanna is Karta of H.U.F. consisting of himself and his two brothers. He furnishes the following particulars of income:

(*i*) Mr. V. Ramanna, Karta's younger brother is manager of M/s Steel Ltd. and he received Rs. 20,000 as salary.

(*ii*) The family business profit was Rs. 40,000. Mr. K Ramanna is partner of a PFAOP in representative capacity and 1/2 share of profits received from such PFAOP is Rs. 4,000. Mr. D. Ramanna, the 3rd brother is a lawyer and his professional income is Rs. 10,000.

(*iii*) The family has ancestral house (self-occupied) whose rental value is Rs. 21,000 p.a. Another house, which was bought in the name of Mr. D. Ramanna out of family funds has annual letting value Rs. 9,000. Taxes paid in respect of these houses are Rs. 2,100 and Rs. 900 respectively.

(*iv*) Rs. 60,000, 8% Debentures of a company purchased by Mr. V. Ramanna out of his salary savings and Rs. 8,000 received as net interest on debentures of a company which were purchased out of family funds.

(*v*) Dividend of Rs. 5,000 received by Mrs. K. Ramanna out of her Stridhan and Rs. 3,200 (Net) on shares of a Company, purchased out of family funds.

Calculate the total income of the H.U.F.

[**Hints:** House Property let out 6,480, self-occupied NIL, Business Income 44,000; other sources 14,000; GTI 64,480; Deduction u/s 80L 4,000; Total Income 60,480. Salary received by V. Ramanna, Professional Income of D. Ramanna, Dividend received by Mrs. Ramanna are their individual incomes.] [P–6]

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Q. No. 3

Mr. G.R. Trivedi, Karta of a H.U.F. furnished the following particulars of income of the H.U.F. for the previous year ending 31st March, 1997:

(*i*) The H.U.F. owned flats in New Delhi, one of which has been occupied by the family for its own residence while the other has been let out for residential purposes at a rent of Rs. 1,000 a month, other particulars relating to the two flats are given below:

	Flat let-out	*Flat self-occupied*
(*a*) Municipal valuation	8,000	10,000
(*b*) Date of construction	1-10-1984	1-10-1991
(*c*) Interest paid to bank on money borrowed for construction of the two flats	1,000	2,000
(*d*) Interest paid on mortgage for daughter's marriage	600	—
(*e*) Collection charges	120	—
(*f*) Repairs	—	3,000
(*g*) Ground rent	100	100
(*h*) Municipal taxes	1,600	2,000

(*ii*) The family owned shares in a number of Indian companies. The gross dividend income received by the family amounted to Rs. 2,000 against which the assessee claimed the following deductions:

(*a*) Interest on money borrowed and invested in the shares Rs. 200.

(*b*) Collection charges paid to a bank Rs. 100.

(*iii*) The interest from deposits in banks during the previous year amounted to Rs. 2,000.

(*iv*) The H.U.F. during the previous year 1996-97 [C.I.I. = 305] sold shares acquired by it in 1990-91. [C.I.I. = 182] The cost of acquisition and sale price were respectively Rs. 22,000 and Rs. 30,600. For the sale of the shares, the family paid a brokerage of Rs. 600.

(*v*) A plot of land meant for house construction in Delhi purchased by the family on 1st October 1982 [C.I.I. for 1982-83 was 109] for Rs. 40,000 was sold by it on 1st October 1996 for Rs. 1,19,000. [C.I.I. for 1996-97 was 305] For the sale of the plot, the family incurred the following expenses:

(*i*) Advertisement	Rs. 100
(*ii*) Brokerage	Rs. 800
(*iii*) Stamp duty	Rs. 3,100

(*vi*) The family earned during the previous year Rs. 20,000 as prize money on Maharashtra State Lottery tickets. It purchased one thousand tickets of Rs. one each during the previous year and only one of them secured the prize of Rs. 20,000.

Compute the total income of H.U.F.

[Hints. HP Income Rs. 5,220 L.T.C. Gain (plot) Rs. 2,881; L.T.C. Loss (shares) Rs. 3,967; L.T.C. loss C/F Rs. 1,086; Other sources Rs. 18,700 Deduction u/s 80L Rs. 3,700 Total income Rs. 20,220] [P-10]

Q. No. 4

Sanjay Chopra, his two brothers and major son constitute an H.U.F. and the following statement of income has been submitted by them for assessment purposes :

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(*a*) Profit from business carried on by the karta in the account and on behalf of H.U.F. Rs. 1,80,000 (after deducting Rs. 6,000 paid to Vijay a member of the H.U.F. for working as travelling salesman and Rs. 20,000 paid to Sanjay Chopra for managing the affairs of the business.)

(*b*) The family owns a house with the rental value of Rs. 10,000, local charges in respect of this being Rs. 500. It is used for residence of the family. Mr. Chopra has created a charge on this house for payment of Rs. 5,000 p.a. to his sister. Fire insurance premium paid is Rs. 100 and theft insurance Rs. 200.

(*c*) The H.U.F. sold another house for Rs. 5,00,000 on 10th April, 1996 (Cost inflation index in 1996-97 was 305) which was acquired in 1955. Its fair market value on 1 April 1981 was Rs. 2,60,000. [C.I.I. for 1981-82 was 100]

(*d*) Loss of stock in trade occasioned by enemy action Rs. 5,000.

(*e*) Sanjay Chopra wins a prize of Rs. 50,000 in Rajasthan State Lottery and claims it as his personal winnings. It is on record that the ticket was bought in his name though the rupee had been spent from the cash box of the business.

(*f*) Dividend on shares Rs. 5,000 (gross) interest on debentures Rs. 10,000 and interest on Govt. securities held by family was Rs. 4,000.

Compute total income of the family for the assessment year 1997-98 giving sufficient explanation for each item. *(B.Com. Panjab April, 1994)*

[**Hints :** Profits & Gains Rs. 1,75,000; Other Sources Rs. 19,000; Lottery prize individual income ; Deduction u/s 80 L Rs. 9,000 Total Income Rs. 1,85,000 L.T.C. Loss to be C/F Rs. 2,93,000] [P-11]

Q. No. 5

A is the karta of a Hindu Undivided Family. The family consists of A and his two brothers. B and C, as co-parceners. The family and the co-parceners has the following incomes and investments for the year ending 31st March, 1997 :—

	Rs.
(*i*) Salary of B as manager of a company	82,000
(*ii*) Interest on government securities :	
(*a*) Investment made in the name of B (made out of his salary income)	38,400
(*b*) Investment made in the name of A (made out of family funds)	6,000
(*iii*) Income from house property :	
(*a*) Municipal value of the ancestral house occupied by the family for residential purposes	17,800
(*b*) Rent received from a house in the name of A (purchased out of family funds)	34,400
(*iv*) Income from business/profession :	
(*a*) Profit from family business	4,18,700
(*b*) Income from profession as lawyer carried on by C	1,29,200
(*v*) Income from shares in the Indian company (gross) :	
(*a*) On shares purchased in the name of A out of family funds	26,000
(*b*) On shares purchased in the name of A's wife out of her Stridhan	13,400

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(*vi*) The family has paid a sum of Rs. 45,000 towards life insurance premium on the life of its members. Sum assured is Rs. 4,00,000 .

(*vii*) The family has deposited a sum of Rs. 4,000 in the National Savings Scheme, 1992.

(*viii*) The family has paid health insurance premium of Rs. 2,000 by cheque under mediclaim.

Compute the taxable income of the Hindu Undivided Family for the assessement year 1997-98. *[Company Secretary Inter June, 1992]*

[**Hints :** H.P. Income Rs. 27,520, P & G Rs. 418,700; Other sources Rs. 32,000; Total Income Rs. 461,220 Tax payable Rs. 1,57,488] [P-7]

Q. No. 6

Mr. Inamdar, the Karta of a H.U.F., has prepared the following Profit and Loss Account for the year ending 31st March, 1997 :

	Rs.		Rs.
To Establishment expenses	22,000	By Gross profit	1,55,000
" Rent	15,000	" Income tax refund	3,000
" Household expenses	17,000	" Bad debtors recovered	5,000
" Income Tax and Wealth tax	10,700	" Agricultural income	7,000
" Gifts and presents	4,500		
" Charities (donations to approved Institutions)	4,300		
" Loss on sale of car	3,200		
" L.I. premium	7,300		
" Interest on loan from Karta	8,800		
" Audit fees	1,000		
" Provision for Depreciation	11,000		
" Difference in Trial Balance	200		
" Net Profit	65,000		
"	1,70,000		1,70,000

Compute the income from business for the Assessment year 1997-98 after taking into account the following :—

1. Establishment expenses include salary to the Karta Rs. 5,000 and to another member of H.U.F. Rs. 5,000.
2. Rent includes rent for the residence of the H.U.F. Rs. 6,000.
3. Car was used for personal purposes.
4. Depreciation allowed as per rules is Rs. 9,000.
5. Bad debts recovered include Rs. 2,000 allowed earlier.

[Karnataka B.Com. April, 1995]

[**Hints :** Interest and salary paid to Karta or any member of H.U.F. is allowed. Rent for residence of H.U.F. disallowed. Business Income Rs. 1,07,200] [P-8]

Q. No. 7

Rajesh and Bros. is a Hindu undivided family of which Rajesh is the Karta. The Income of the family and of the members for the year ending March, 31, 1997 was as under :—

1. The family runs a hotel. Net profit as per Profit and Loss A/c is Rs. 60,000. The profit is arrived at after debiting the following :—

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Salary to karta Rs. 12,000. Salary to Suresh (a member of the family) Rs. 22,000. Loss on gold speculation Rs. 8,000. Loss on horse race Rs. 5,000. Life Insurance premium paid on the life of Karta Rs. 2,000. Contribution to Unit Linked Insurance Policy Rs. 4,000. Donations to political parties Rs. 2,000; to National Defence Fund Rs. 3,000; to approved institution Rs. 1,000 and to Prime Minister's National Relief Fund Rs. 7,000.

The following were credited to Profit and Loss Account :

Profit on silver speculation Rs. 22,000. Winning from lotteries (net) Rs. 60,000. Dividend from a company (net) Rs. 8,000. Interest on government securities (net) Rs. 2,700. (After TDS @ 10%)

2. Dinesh, another member of the family, is a government employee and his Salary income during the year is Rs. 48,000. He has no other income.
3. The Assessing Officer considers that salary to Suresh is not commercially justifiable beyond Rs. 15,000 p.a.

Compute the total Income of the family and tax liability for the Assessment year 1997-98. *[Karnataka B.Com. 1994]*

[**Hints :** Business Profit Rs. 6,300; Speculation gain Rs. 14,000; Other sources Rs. 1,08,000; Deductions u/s 80L Rs. 13,000; u/s 80G Rs. 9,000; Total Income Rs. 1,06,300. Tax on H.U.F. Rs. 26,520 less rebate u/s 88 Rs. 1,200] [P-9]

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3 ASSESSMENT OF FIRMS

What is partnership ?— Past treatment — New treatment of firms — Types of firms—(A) Partnership firm assessed as firm (PFAF)— (B) Partnership firm assessed as Association of persons (PFAOP)

(A) PFAF's Business Income—Limits on salary, commission, bonus, remuneration, interest received by partners u/s 40(b)—Computation of PFAF's Total income—PFAF's Tax-treatment of share of income from PFAF—Treatment of remuneration received by partners from PFAF.

(B) PFAOP's Business Income—Computation of Total income—Allocation of PFAOP's total income—Treatment of share of income received by partners of PFAOP. Illustrations and questions.

What is Partnership ?

The terms 'Partnership', 'Partner' and 'Firm' as defined under section 2 (23) of Income Tax Act, have the same meaning as assigned to them in the Indian Partnership Act, 1932.

Section 4 of the India Partnership Act has defined the word 'Partnership' as "the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all".

From this definition, the following points emerge :

(*a*) That partnership is an association of two or more persons.

(*b*) There must be an agreement entered into by all persons.

(*c*) The agreement is to carry on some business.

(*d*) The business to be carried on by all or by any one of them acting on behalf of all and for the benefit of all.

(*e*) The agreement is to share the profits and losses of business.

The term 'partner' is defined as any person who has entered into partnership. Partners entering into a contract with one another are called individually as partners and collectively 'a firm' and the name under which their business is carried on is called the firm's name. The word 'partner' shall also include any person who, being a minor has been admitted to the benefits of partnership.

The term 'firm' means the entity which comes into existence as a result of partnership agreement.

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(A) PARTNERSHIP FIRM ASSESSED AS FIRM [PFAF]

The Finance Act 1992 has introduced a new approach to taxation of firms. The firms have been given a separate status with separate rate of tax. Share of income received by partners is not to be added in their individual income and as such it is exempted. Only that entity created by partnership is to be treated as firm which Income-tax Act 1961 accepts as firm. All other entities are to be treated as Association of persons. (A.O.P)

Which firm is to be assessed as firm ? [section 184]

A firm shall be assessed as firm for its assessment under this Act if —

(*a*) A partnership is evidenced by an instrument, and

(*b*) The individual shares of the partners are specified in that instrument.

Instrument of partnership. It is the written partnership agreement entered into by partners. It has to be signed and certified by all the existing partners (except minors). In case firm has been dissolved before filing of return of income—it should be signed by all those persons who were partners in the firm immediately before its dissolution and in case partner has died the instrument must be signed by his legal representatives immediately before its dissolution as in case partner has died the instrument must be signed by his legal representatives.

When instrument of partnership is to be submitted ? The section 184(2) of the Act provides that a certified copy of the instrument of partnership must accompany the return of the income of the firm of the previous year relevant to the assessment year 1993-94 or the assessment year in respect of which assessment as a firm is first sought.

Change in Constitution ? When a firm is assessed as firm for any assessment year it shall be assessed in same capacity for every subsequent year unless there is change in the constitution of firm or in the share of partners as evidenced by the instrument of partnership submitted along with return for first assessment. [section 184(3)]

In case any change has taken place during the previous year the firm shall furnish a certified copy for the previous year in which such change takes place. In such case the firm will continue to be assessed as firm. [section 184(4)]

Meaning of change in constitution [section 187]

In following two circumstances a change can occur in the constitution of firm :

(*a*) If one or more of the partners cease to be partners (one or more partners quit or retire from the firm) or one or more new partners are admitted but one or more of the old partners are still continuing with the firm after the change.

(*b*) where all the partners continue with a change in their respective shares or in the shares of some of them.

In other words, if during the previous year one or more partners but not all have retired or one or more partners have joined the partnership or there is a change in the profit sharing ratio of the partners, it amounts to a change in the constitution of the firm.

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Succession of One Firm by Another Firm (Sec. 188)

When a firm is succeeded by another firm it results into the finishing of the firm or predecessor firm gives birth to a new firm. As it is not covered by section 187, so separate assessments shall be made on the predecessor firm on its income earned before the transfer of ownership and the successor firm shall be assessed on its income after the transfer of ownership.

Liability of partners for tax payable by firm [section 188A]

It is the joint as well as several liability of all those persons who were partners of the firm during relevant previous year or in case of death of a partner their legal representatives to pay the amount of tax, interest or penalty or other sum payable by the firm for the relevant assessment year under all the provisions of this Act.

Firm Dissolved or Business Discontinued

Where any firm is dissolved or business discontinued, the firm shall be assessed by the Assessing Officer on its total income as if no such discontinuance or dissolution had taken place. The notices may be issued in the name of the dissolved firm and the assessment be made in the name of the discontinued firm. [section 189(1)].

In case during the proceedings before Assessing officer, or the Deputy Commissioner (Appeals) or the Commissioner (Appeals) the firm is found guilty of any acts as given u/s 271 to 275 the penalty can be imposed on such firms. [section 189(2)]

Every person who at the time of such discontinuance or dissolution was a partner of the firm, or the legal representative of any such person who is deceased, shall be jointly and severally liable for the amount of tax, penalty and any other sum payable under the provisions of this Act. [section 189(3)]

Where such discontinuance or dissolution takes place after any proceedings in respect of an assessment year have commenced the proceedings may be continued for the persons referred above from the stage at which they stood at the time of such dissolution or discontinuance. [section 189(4)]

Firm to be assessed as A.O.P [section 184(5)]

In case there is either on the part of the firm or on the part of the partners, there is some failure and as a result such firm is subject to best judgement assessment u/s 144, the firm shall not be assessed as firm in that assessment year and will be subject to treatment as an Association of persons.

Treatment as an A.O.P [section 185]

In case a firm does not comply with the provisions of section 184 for any assessment year, the firm shall be assessed in the same manner as an association of persons is assessed.

COMPUTATION OF FIRM'S [PFAF's] BUSINESS INCOME

5. Adjustment of Net Profit as per Profit & Loss Account of the firm

(*a*) While calculating firms business profit the provisions as given u/s 28 to 44 as given in Chapter. *Profits & Gains of Business or Profession I & II* in part II of this book are applicable.

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(*b*) Section 40(b) lays down following rules regarding payment of salary, commission, or remuneration to working partners and interest on capital to all partners. These rules are :

(*i*) Any payment of salary, commission or remuneration paid to a partner who is not a working partner, is *disallowed.*

(*ii*) Any remuneration paid to a working partner which is not authorised by or which is not in accordance with terms of partnership deed (instrument of partnership) is *disallowed.*

(*iii*) Any interest paid to partners according to terms of partnership deed is *allowed* provided rate of interest does not exceed 18% p.a. Exess is *disallowed.*

(*iv*) Any interest paid to partner which is not authorised by or is not in accordance with partnership deed is *disallowed.*

(*v*) In case interest or remuneration is paid to a partner and is authorised by partnership deed but relates to the period prior to the date of such deed and it was also not authorised by any earlier deed, it shall be *disallowed.*

(*vi*) In case any payment for remuneration is made to one or more working partners during the previous year, it is *allowed* upto limits given below. *Excess is disallowed.*

LIMITS ON PAYMENT OF REMUNERATION [Section 40(b)]

1. *In case of professional firms (as defined u/s 44 AA)*

	Amt. allowed
(*a*) On the first Rs. 1,00,000 of the book profit or in case of loss	Rs. 50,000 or at the rate of 90% of the book profits whichever is more
(*b*) On the next Rs. 1,00,000 of the book profits	@ 60%
(*c*) On the balance of the book profits	@ 40%

2. *In case of any other firms*

(*a*) On the first Rs. 75,000 of the book profits or in case of loss	Rs. 50,000, or at the rate of 90% of book profits whichever is more
(*b*) On the next Rs. 75,000 of the book profits	@ 60%
(*c*) On the balance of the book profits	@ 40%

The above limits can be expressed in following in owner :—

1. In case a firm (Whether professional or non professional) has loss or it has profit but total remuneration paid to working partners as per instrument of partnership does not exceed Rs. 50,000—Actual remuneration or Rs. 50,000 per whichever is less is allowed.
2. In case total remuneration is more than Rs. 50,000 and firm is carrying on profession it is allowed upto

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(*a*) Actual remuneration to all working partners as per instrument of partnership.

OR

(*b*) An amount equal to [90% of first Rs. 1,00,000 + 60% of next Rs. 1,00,000 + 40% of Balance Book Profits] whichever is less.

3. In case firm is non-professional firm and total remuneration paid is more than Rs. 50,000, it is allowed upto

(*a*) Actual remuneration to all working partners as per deed.

OR

(*b*) An amount equal to [90% of first Rs. 75,000 + 60% of next Rs. 75,000 + 40% of balance book profits] whichever is less.

Certain Explanations

1. In case an individual is partner in a representative capacity for the benefit of another person, such partner is called *partner in representative capacity* and the other person is called person so represented.
Any interest paid to partner in representative capacity shall be subject to aforesaid limits but any interest paid to him in his individual capacity (as creditor) shall not be subject to above mentioned limits.

2. Any interest paid to an individual (who is neither partner in representative capacity nor in personal capacity) and such interest is received by him on behalf of or for the benefit of any other person, it shall not be subject to the aforesaid limits.

3. The term *Book Profit* means the net profit as shown in the Profit & Loss Account for the relevant previous year computed according to provisions given u/s 28 to 44 of the Act and after adding back the full amount of remuneration given to partners (as referred to in limits above).

4. The term working partner means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner.

Treatment of interest, salary, bonus, commission or remuneration received by partners [section 28 (*v*)]

In case any interest, salary, bonus, commission or remuneration is received by a partner from firm, it shall be his taxable income under the head Profits and Gains. In case any amount of interest, salary, bonus or commission or remuneration has been subjected to limits u/s 40 (*b*), the income of the partners shall be adjusted accordingly.

COMPUTATION OF FIRM'S [PFAF's] TOTAL INCOME

(*i*) Income is to be calculated head wise. Firm cannot have any income under the head 'salaries'.

(*ii*) Firm can have house property which is let out but not a self occupied one. For let out house property income is to be computed in the same manner as is given under the head *Income from House Property*'

(*iii*) Profits and Gain from business or profession are to be computed in the same manner as given earlier in this chapter.

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(*iv*) Capital Gains are to be computed in the same manner as given under the head "Capital Gains" but exemptions u/s 54, 54B and 54F are not allowed.

(*v*) 'Income from other sources'—is to be computed in the same manner as is given under the head "Income from other sources".

(*vi*) (*a*) Set off of losses is to be done as per rules given u/s 70 and 71 of the Act. The carry forward of losses is also to be done in accordance with rules given u/s 72, 73 and 74.

(*b*) In case firm had loss for any assessment year upto 1992-93 which remained unadjusted from firms income and was allocated amongst partners and partners were also unable to adjust it such unadjusted portion of loss can be set off from firm's income (as per rules of section 70,71,72,73,74A) and to be carried forward provided the partner continues to be the partner of said firm. [section 75]

(*c*) Where a change has occured in the constitution of a firm, the proportionate share of loss of retired or deceased partner can be set off or carried forward to be set off only upto his share of income in that firm in respect of that previous year. [section 78(1)]

(*d*) To avail the benefit of carry forward of loss it is essential to file return of loss as required u/s 139(3). [section 80]

(*vii*) *Deductions u/s 80 out of Gross total income*—A firm can claim deductions u/s 80G for donations, u/s 80GGA for contribution to certain funds, u/s 80HHB for profits from foreign contracts, u/s 80HHC for export profits, u/s 80HHD for providing services to foreign tourists, u/s 80HHE for profit from export of computer software, u/s 80IA for new industrial undertaking, u/s 80JJ for profits from business of poultry farmings u/s 80O for royalty received for use of patents outside India; and u/s 80 Q for profits from publishing business.

Firm is not allowed any other deduction including 80L for divided etc.

FIRM'S [PFAF's] TAX

With effect from assessment year 1993-94 the firm is to be assessed to tax at a flat rate of 40% with no exemption limit. But in case total income includes long term capital gain, the income will be split up in two parts *i.e.*

(*a*) Long term Capital Gain; and

(*b*) Balance Total Income.

The tax will be calculated at the rate of—

(*a*) 20% of long term capital gain; and

(*b*) 40% of balance total income.

SHARE OF INCOME FROM FIRM [PFAF]

The firm's total income need not be allocated amongst partners as their share in the total income of a firm (which has been assessed as firm) shall be fully exempted u/s 10(2A) and shall not be included in their individual income.

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The exemption will be admissible only on such amount of share from firm which is in accordance with the partnership deed.

Illustration 1. The Profit and Loss Account of a firm in which the partners X, Y and Z share profits and losses in the ratio of 5 : 4 : 1 respectively discloses profit of Rs. 80,625 for accounting year ending 31st March 1997.

Debits	Rs.	*Credits*	Rs.
Donation to National Defence Fund	11,000	Capital gain on sale of Scrap machinery	5,000
Salary to Partners :		Dividend after deduction of tax	
X Rs. 15,000		at source Rs. 5,000	20,000
Y Rs. 19,000		Interest on Securities	
Z Rs. 22,000		(Gross)	3,500
	56,000		
Commission to X	6,000		
Office Rent (Paid to Y)	12,000		

Compute the total income of the firm for the assessment year 1997-98. The firm has submitted certified copy of instrument of partnership along with return and it provides for payment of salary, commission to working partners X,Y and Z as per above.

Solution

Computation of firm's business profit

	Rs.	Rs.
Net Profit as per P & L A/c		80,625
Add inadmissible expenses		
Donation to N.D.F	11,000	
Salary to partners	56,000	
Commission to X	6,000	
		73,000
		1,53,625
Less: Incomes not taxable under this head		
Profit on sale of scrap (S.T.C. Gain)	5,000	
Dividend	20,000	
Interest on Securities	3,500	
		28,500
Book Profits		1,25,125
Less Expenses allowed u/s 40(b)		
Actual Salary to partners Rs. 56,000		
Commission to partners Rs. 6,000		
	62,000	

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OR

90% of Book Profits upto Rs. 75,000 + 60%, of 50,125 (*i.e.* 67,500 + 30,075)	97,575	
Whichever is less		62,000
Firm's Business Profit		63,125

Computation of Firm's total Income

Business Income		63,125
Capital Gain (Short Term)		5,000
Other sources :		
Dividend (20,000 + 5,000)	25,000	
Interest on Securities	3,500	
		28,500
Gross Total Income		96,625
Deduction u/s 80G : Donation to N.D.F. Rs. 11,000		5,500
Rate 50%		
Total Income		91,125

Rounded off to Rs. 91,130

Individual income of partners

1. Share of income received by each partner from their firm shall be fully exempted u/s 10 (2A).
2. Salary and Commission received by partners will be their taxable income under the head profits & Gains of business or profession.

Illustration 2. Calculate firm's income under the head profits & gains for the assessment year 1997-98 from information given below:

		Rs.
Net Profit as per P & L A/c (after debiting the following)		20,000
Salary to	A	60,000
	B	40,000
Commission to	A	20,000
Interest on Capital @ 21%		
	To A	14,000
	To B	7,000

The payments to partners A & B (who are working partners) have been made in accordance with partnership deed whose certified copy has been submitted along with return of income for the assessment year 1997-98. Also compute the individual income of partner A & B which is taxable under the head profits & Gains.

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Solution

(a) Computation of firm's business income

	Rs.	Rs.
Net Profit as per P & L A/c		20,000
Add inadmissible expenses		
Salary to A	60,000	
Salary to B	40,000	
Commission to A	20,000	
Interest on Capital (Excess over 18%) (21,000 × 18/21)	3,000	
		1,23,000
Book Profits		1,43,000
Less : Expenses allowed u/s 40 (b)		
Salary to working partners	1,00,000	
Commission to partner	20,000	
Actual Total	1,20,000	
OR		
[90% of 75,000+60% of 68,000 = 67,500+40,800] 1,08,300 whichever is less		1,08,300
Taxable Business Profits of firm		34,700

(b) Individual income of partners

(*i*) Share of income from this firm will not be included in the individual income of partners as it is exempted u/s 10(2A)

(*ii*) Salary and Commission received by A & B will be taxable (as under) income under the head profit & Gains

Remuneration taxable in the hands of partners under the head *'Profits and Gains'*

	Rs.
Partner 'A'	
Remuneration – salary [60,000 × 1,08,300/1,20,000]	54,150
Commission [20,000 × 1,08,300/1,20,000]	18,050
Interest @ 18% [14,000 × 18/21]	12,000
	84,200
Partner 'B'	
Remuneration [40,000 × 1,08,300/1,20,000]	36,100
Interest @ 18% [7,000 × 18/21]	6,000
	42,100

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Illustration 3. A,B and C are partners in a firm assessed as firm sharing profits and losses in the proportion of 3 : 2 : 1

The firm's Profit and Loss Account for the year ended 31st March, 1997 showed a net profit of Rs.1,17,360 after debiting *inter-alia* the following amounts :

(*i*) Salary of Rs. 4,000 paid to C.

(*ii*) Rent of Rs. 9,000 paid to A for the portion of building owned by A in which the firm's office was situated.

(*iii*) Interest on capital @ 15% is Rs. 1,000; Rs. 2,000 and Rs. 3,000 to A, B and C respectively.

(*iv*) Commission on sale to B, Rs. 1,000.

(*v*) Expenses on current repairs of the business premises belonging to partner A, Rs. 1,000.

(*vi*) Donation to approved bodies, Rs. 5,000.

The net profit of Rs. 1,17,360 included Rs. 9,360 from interest on Government securities (after deduction of tax at source Rs. 1,040)

Compute firm's total income for the assessment year 1997-98. The deed was submitted along with return and it provides for salary to C Rs. 4,000 p.a. and interest on capital to partners @ 15% p.a.

Also compute partner's income chargeable to tax under the head Profits and Gains"

Solution. *Computation of firm's Business Income*

	Rs.	Rs.
Profits as per given in the P & L A/c		1,17,360
Add : *Inadmissible expenses*		
Salary to C	4,000	
Commission to B	1,000	
Expenses on repairs	1,000	
Donations	5,000	11,000
		1,28,360
Less : Income not taxable under this head		9,360
Interest on Govt. Securities		
Less : Allowable remuneration u/s 40 (*b*)		1,19,000
Salary to C		4,000
Firm's Business Profit		1,15,000
Firm's Total Income		
Income from other sources: Interest on Govt. securities (9,360 + 1,040)		10,400
Income from business		1,15,000
Gross Total Income		1,25,400
Deduction u/s 80G: Donations Rs. 5,000: 50%		2,500
Total Income		1,22,900

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Computation of Firm's Tax

Total Income Rs. 1,22,900

Tax @ 40% Rs. 49,160

Partners income under the head profits and gains

A's income (Interest)		Rs. 1,000
B's income (Interest)		Rs. 2,000
C's income (Interest)	Rs. 3,000	
Salary	Rs. 4,000	
	———	7,000

Note 1. Commission paid to B has been disallowed as it is not authorised by deed. Share of partner from firm is fully exempted u/s 10(2A).

(B) PARTNERSHIP FIRM ASSESSED AS A.O.P. [PFAOP]

Upto assessment year 1992-93 the Income-tax Act 1961 provided for treatment of two types of firms—Registered under Income-tax Act as regd. Firm and not registered under income-tax Act as Unregd firm. But with effect from assessment year 1993-94 the Act provides only one type of firms—firms assessed as firm u/s 184. All other such entities are to be treated as A.O.P. Hence a firm which is not assessed as firms u/s 184 will be called as P.F.A.O.P. and treated alike for assessment purposes.

Computation of PFAOP's Business Income

While calculating the business income of P.F.A.O.P., the provisions as given u/s 28 to 44 in chapter Profits & Gains of Business or Profession I and II (See Part II of this book) are applicable.

2. Section 40 (*ba*) lays down following rules disallowing payment of interest, salary, bonus, commission or remuneration by what ever name called :—
   (*a*) In case an P.F.A.O.P. makes payment of any interest, salary, bonus, commission or remuneration by whatever name called, such payments are fully disallowed.
   (*b*) In case any interest is paid to a member of firm assessed as AOP and some amount of interest is received from such member, only difference is disallowed.
   (*c*) In case an individual is a member (member in representative Capacity) P.F.A.O.P. on behalf of or for the benefit of any other person (person so represented) :—
      (*i*) Interest paid by firm assessed as AOP to such individual, or by such individual to firm assessed as AOP otherwise than in representative capacity, the above clauses (*a*) and (*b*) shall not be applicable.
      (*ii*) Interest paid by a firm assessed as AOP to such individual or by such individual to or firm assessed as AOP in representative capacity classes (*a*) and (*b*) shall be applicable.
   (*d*) In case an individual is member of firm assessed as AOP on behalf of another person but not in representative capacity, interest paid to him will not come under the classes (*a*) and (*b*) above.

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Computation of PFAOP's total income

(*i*) Income of P.F.A.O.P. is calculated head wise. It cannot have any income under the head "Salaries".

(*ii*) In case of house property rules given under the head "Income from House Property" are applicable. It cannot have self occupied house.

(*iii*) Profits & Gains from Business or Profession are to be computed in the same manner as given earlier in this chapter.

(*iv*) Income under the head "Capital Gains" is to be computed in the same manner as given in the chapter Capital Gains but exemptions u/s 54, 54B and 54F are not allowed.

(*v*) Income from other sources is to be computed in the same manner as given under the head "Income from other Sources".

(*vi*) Set off and carry forward and set off of losses is to be done as per provisions of section 70 to 74 of the Act.

(*vii*) Deductions u/s 80 can be claimed. The deductions which can be claimed by P.F.A.O.P. are u/s 80 G, u/s 80 GGA, u/s 80 HHB, u/s 80 HHC, u/s 80 HHD, u/s 80 HHE, u/s 80 IA, u/s 80 JJ, and u/s 80 Q. Other deductions u/s 80 are not allowed.

RATES OF TAX FOR PFAOP/AOP [u/s 167B]
(Assessment year 1997-98)

A. *Where shares of members of PFAOP/AOP are not known or are indeterminate :*

1. In case PFAOP/AOP (excluding a company, a co-operative society or a society registered under Societies Act 1860) where shares of its members are not known or are indeterminate and it does not have any such member whose income is taxable at a rate higher than MMR (Maximum Marginal Rate)—the total income of such PFAOP/AOP shall be taxable at MMR *i.e.* 40%.
2. In the above case if PFAOP/AOP has any member whose individual income is taxable at a rate higher than MMR—the total income on such PFAOP/AOP shall be taxable at such higher rate.

B. *Where shares of members of PFAOP/AOP are known or are determinate :*

1. In case total income [excluding share from PFAOP/AOP] of any member of PFAOP/AOP does not exceed the exempted limit *i.e.* Rs. 40,000—the total income of such PFAOP/AOP shall be assessed to tax at same rates as are applicable to an applicable.
2. In case total income of any member of PFAOP/AOP exceeds the exempted limit—the total income of such PFAOP/AOP shall be assessed at MMR.
3. In case PFAOP/AOP has any member whose total income (in case of companies only) is taxable at a rate higher than MMR, the total income of such PFAOP/AOP shall be split up in two parts—

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(*i*) the share of income of the member whose income is assessable at a rate higher than MMR, this part of total income of PFAOP/AOP shall be taxable at such higher rate.

(*ii*) and balance total income of PFAOP/AOP shall be assessed to tax at MMR.

Allocation Of P.F.A.O.P's Total Income [Section 67A]

1. (*a*) Any interest, salary, commission or other remuneration paid to any member in respect of the previous year, shall be deducted from the total income of the P.F.A.O.P. and the balance ascertained is apportioned amongst the members in the profit sharing ratio. It has been observed by the Supreme Court in case [*CIT v. Chindambram Pilai (1977) 106 ITR 292*] that the salary received by a member from the P.F.A.O.P. in which he is a member cannot be regarded in any way as having a source different from that of his share in the profits of the P.F.A.O.P. he receives.

(*b*) In case any interest on capital is paid to partners and interest on drawings is received from partners, only difference of these two is to be allocated.

(*c*) Where the amount apportioned to the member is a profit, any salary, interest, commission or other remuneration paid to the member by the P.F.A.O.P. shall be added to that amount (profit apportioned) and the total of all these amounts shall be treated as that member's share in the Income of the P.F.A.O.P.

(*d*) Where the amount apportioned comes to be a loss, any salary, interest, commission or other remuneration paid to the partners of the P.F.A.O.P. shall be adjusted against the amount of loss so apportioned. If after the adjustment the result is positive, it shall be treated as the members share in the income of the P.F.A.O.P.

(*e*) P.F.A.O.P's tax is not to be deducted out of total income for allocation purposes.

2. The share of a member whether income or loss as computed under sub-section (1) shall, for the purposes of assessment, be apportioned under the various heads of income in the same manner in which the income or loss of the P.F.A.O.P. has been determined under each head of income.

3. Any interest paid by a partner on capital borrowed by him for the purpose of investment in the P.F.A.O.P., shall be deducted from the share of his income computed under the head 'Profits and Gains' of business or profession.

Treatment of Share of Income Received By Members Of P.F.A.O.P.

The share of income received by a member from a P.F.A.O.P. shall be treated as under :—

1. In case a firm assessed as AOP is chargeable to tax on its total income at maximum marginal rate or any other higher rate, the share of members

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firm such firm assessed as AOP shall not be included in their individual income. It happens only when shares of members are unknown or indeterminate.

2. In case share of members of firm assessed as AOP are known or can be determined, the share received by members from such firm assessed as AOP shall be fully added in their individual income.
3. In case no income-tax is payable on firm assessed as AOP's total income, the share of income of members of such firm assessed as AOP shall be fully added in their individual income.

Rabate of Tax u/s 86

1. In case total income of PFAOP/AOP is **not** taxable at MMR or any other rate higher than MMR—the share of income of a member of PFAOP/AOP shall be added in his total income **and shall be eligible for rebate of tax at average rate on such share.**
2. In case total income of PFAOP/AOP is taxable at MMR or a higher rate —the share of income of a member from such PFAOP/AOP shall **not be included in the total income of such member.**
3. In case total income of PFAOP/AOP in not taxable at all—the share of income of a member from such PFAOP/AOP shall be **fully added in the individual income of such member and is fully taxable. No rebate of tax in this case.**
4. The term average rate of income-tax means the rate computed in following manner [Section 2(10)] :—
   = Total Income Tax × 100/Total Income

Treatment of P.F.A.O.P's Loss

1. *Setoff*—P.F.A.O.P's losses are to be set off as per rules given u/s 70 and 71.

2. *Carry Forward*—Only firm assessed as AOP can carry forward its loss as per provisions of section 72, 73, and 74. It is not allocated amongst members as members cannot adjust their share of loss from their individual income.

Illustration 4. A, B and C are partners in a firm assessed as AOP sharing profits and losses equally. The following is the profit and loss account of the firm.

	Rs.		Rs.
To Manufacturing Expenses	9,000	By Gross Sales	50,000
" Establishment Expenses	6,000	" Interest on Securities (Gross)	3,000
" Depreciation	3,000		
" Sundry Expenses	4,000		
" Salary to A	6,000		
" Commission to B	4,000		
" Interest on Capital			
A 1,000			
B 2,000			
C 3,000			
	6,000		

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To Net Profit			
	A 5,000		
	B 5,000		
	C 5,000		
		15,000	
		53,000	53,000

Compute the Income of the firm and allocate it amongst its partners.

Solution

Computation of P.F.A.O.P's Business income

		Rs.
Profits as given in the Profit and Loss Account		15,000
Add: Inadmissible items :	Rs.	
Salary to A	6,000	
Commission to B	4,000	
Interest on Capital		
A	1,000	
B	2,000	
C	3,000	
		16,000
		31,000
Less: Income to be treated under a separate head:		
Income from : terest on securities		3,000
P.F.A.O.P's business Income		28,000

P.F.A.O.P's Total Income

Income from other sources: Interest on Securities	3,000
Income from business	28,000
P.F.A.O.P's Total Income	31,000

Note : Tax liability of P.F.A.O.P. is Nil as total income is below exempted limit.

Allocation amongst Partners

		A	B	C
Salary	Rs.	6,000	—	—
Commission	Rs.	—	4,000	—
Interest on Capital	Rs.	1,000	2,000	3,000
Balance of total income dividend amongst the partners in the ratio of 1/3 : 1/3 : 1/3	Rs.	5,000	5,000	5,000
Total	Rs.	12,000	11,000	8,000

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Illustration 5. The folowing is the Profit and Loss Account of a partnership firm assessed as AOP of Mohan, Sohan and Ramesh.

	Rs.		Rs.
To General Expenses	10,000	By Gross Profit	52,000
,, Bad debts	1,000	" Interest on Securities	
,, Establishment Expenses	6,000	(Gross)	6,000
,, Municipal Taxes		" Rent from Property	9,000
(for property let)	250	" Int. On Drawings	
,, Salary to Sohan	6,000	Mohan 1,000	
,, Commission to Ramesh	6,000	Sohan 1,500	
,, Interest on Capital		Ramesh 2,000	
			4,500
Mohan	4,000		
Sohan	4,500		
Ramesh	5,000		
" Depreciation	2,400		
" Bad Debts Reserve	1,000		
" Net Profit			
Mohan	10,140		
Sohan	10,140		
Ramesh	5,070		
	71,500		71,500

Partners are sharing the profit and loss in the ratio of 2 : 2 : 1 respectively. Calculate the total income of the P.F.A.O.P. and allocate it amongst the partners.

Sollution

Computation of Business income of P.F.A.O.P.

	Rs.	Rs.
Profit as given in the Profit and Loss A/c		25,350
Add: Inadmissible items :		
Salary to partner—Sohan	6,000	
Interest on Capital less int. on drawings		
Mohan (4,000 – 1,000)	3,000	
Sohan (4,500 – 1,500)	3,000	
Ramesh (5,000 – 2,000)	3,000	
Commission to Ramesh	6,000	
Bad debts reserve	1,000	
Municipal Taxes related to house property	250	
		22,250
		47,600
Less: Income taxable under separate heads :		
Income from Interest on Securities	6,000	
Income from House Property	9,000	
		15,000
Firm's Business Income		32,600

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Firm's Total Income :

Income from House Property :		
Rental value	9,000	
Less: Municipal Taxes	250	
A.V.	8,750	
Deduction :	1,750	
1/5th of A.V. as repair allowance		7,000
Income from Business		32,600
Income from other sources: Int. on securities		6,000
Total Income		45,600

Allocation amongst partners (2 : 2 : 1)

	Mohan Rs.	Sohan Rs.	Ramesh Rs.
Interest on Capital	4,000	4,500	5,000
Salary	—	6,000	—
Commission	—	—	6,000
Total	4,000	10,500	11,000
Less: Interest on drawings	1,000	1,500	2,000
	3,000	9,000	9,000
Share of business Income (45,600 – 21,000) ratio 2 : 2 : 1	9,840	9,840	4,920
Total	12,840	18,840	13,920

In case the profit and loss account of the A.O.P. shows a loss, then it is adjusted by disallowing those expenses which are not connected with the A.O.P.'s business and also by increasing loss by the amount which was to be allowed but which was left.

The net loss is calculated after allowing or disallowing certain expenses. If the firm is assessed as AOP the net loss is not allocated amongst the partners but the loss is carried forward in the name of the P.F.A.O.P. to be set-off against the P.F.A.O.P's income of future years.

Illustration 6. Bimal, Nirmal and Ashok are partners sharing profit and loss equally. The following is the profit and loss account :

Profit and Loss Account

	Rs.		Rs.
Sundry Expenses	22,000	Gross Profit	22,000
Office expenses	3,000	Interest on Securities (Gross)	3,000
Rent of Premises	1,000		
Commission to Nirmal	2,000	Net loss—	
Interest on Capital		Bimal	7,000
Bimal	3,000	Nirmal	7,000

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Nirmal	3,000	Ashok	7,000
Ashok	3,000		
Salary to Bimal	6,000		
Charity	1,000		
Advertisement Expenses	2,000		
	46,000		46,000

Calculate the total income of the firm assessed as AOP and allocate it amongst the partners.

Solution

Calculation of P.F.A.O.P's income under the head Profits and Gains.

	Rs.	Rs.
Net loss as shown in the profit and loss account		– 21,000
Add: Inadmissible items :		
Commission to Nirmal	2,000	
Interest on capital		
Bimal	3,000	
Nirmal	3,000	
Ashok	3,000	
Salary to Bimal	6,000	
Charity	1,000	
		+ 18,000
		– 3,000
Less: Income to be treated under a separate head :		
Income from interest on securities		– 3,000
Loss from Business		– 6,000
P.F.A.O.P's Total Income :		
Income from other sources: interest on securities		+ 3,000
Loss from business		– 6,000
Net Loss		– 3,000

Note : This loss is not to be allocated as member cannot adjust it from their individual income. Only PFAOP shall carry it forward.

Illustration 7. A, B and C are partners in a P.F.A.O.P. whose Profit and Loss Account is as follows :

	Rs.		Rs.
General Expenses	8,800	Gross Profit	13,800
Salary to A	1,500	Interest on	
Commission to B	4,000	securities (Gross)	2,000
Interest on Capital—		Net Loss A	1,400
A 1,200		B	1,400
C 1,000		C	1,400
	2,200		

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Charity	500	
Bad Debts	600	
Bad Debts Reserve	1,900	
Rent of firm's shop	500	
	20,000	20,000

Calculate Total Income of the firm assessed as AOP and allocate the same amongst partners after considering that the—

Business shop is owned by B.

Solution

Computation of PFAOP's Total Income and its allocation amongst its partners.

	Rs.	Rs.
Loss as shown in the P. & L. A/c		– 4,200
Add: Disallowed items :		
Salary to A	1,500	
Commission to B	4,000	
Interest on Capital—		
A	1,200	
C	1,000	
Charity	500	
Bad debts reserve	1,900	
		+ 10,100
		+ 5,900
Less: Income to be treated under separate head: Interest on securities		2,000
Business profit of the *PFAOP*		3,900
PFAOP's Total Income:		
Income from other sources: Interest on securities		2,000
Income from business		3,900
Total		5,900

Notes : PFAOP's income up to Rs. 40,000 is exempted, so PFAOP's tax liability is NIL.

Allocation amongst Partners :

	A Rs.	B Rs.	C Rs.
Salary	1,500	—	—
Commission	—	4,000	—
Interest on capital	1,200	—	1,000
Share of loss to be allocated in the profit-sharing ratio	– 600	– 600	– 600
Total	+ 2,100	+ 3,400	+ 400

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Note : PFAOP's income which is to be distributed amongst the partners is only Rs. 5,900 whereas Rs. 7,700 were to be distributed according to some agreement amongst the partners. So Rs. 7,700 were distributed, thus resulting into a loss of Rs. 1,800 which was also distributed amongst the partners in their profit-sharing ratio.

Partner's profit-sharing ratio is not given. It is assumed that they share profits and losses equally.

Illustration 8. A, B and C are members of AOP sharing profits and losses in the proportion of 2 : 2 : 1 respectively. Profit and Loss Account for the year is as following:

	Rs.		Rs.
Salaries and Wages	16,000	Gross Profit	50,700
Marketing charges	175	Profit on sale of	
Advertising	325	Motor car	800
General charges	11,700	Profit on sale of	
Legal expenses	2,500	Investments	400
Travelling expenses	1,400		
Interest on Bank loan	150		
Discount	75		
Reserve for Bad Debts	125		
Bad debts written off	80		
Payment to retiring member	1,000		
Interest on capital			
A Rs. 300			
B Rs. 400			
C Rs. 800			
	1,500		
Net Profit	16,870		
	51,900		51,900

Compute the taxable income of the PFAOP and allocate it amongst the partners considering the following:

(*a*) Salaries and wages include a partnership salary of Rs. 500 per month to B;

(*b*) General charges include a sum of Rs. 3,000 paid to save business reputation; and

(*c*) Motor car was used wholly for business purposes. At the time of sale the written down value of the car was Rs. 25,000 while it was sold for Rs. 25,800.

Solution

Computation of P.F.A.O.P. business income.

	Rs.	Rs.
Net profit as per Profit and Loss Account		16,870
Add: Inadmissible items:		
Reserve for bad debts	125	

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Payment to a retiring member	1,000	
Interest on capital—		
A 300		
B 400		
C 800		
	1,500	
Salary to B @ Rs. 500 p.m.	6,000	
		8,625
		25,495
Less: Income to be treated separately:		
Capital Gain (800+400)		1,200
PFAOP's business income		24,295
Computation of total income:		
Profits & Gains : Business Profit		24,295
Capital Gains		
S.T.C. Gains on car	800	
L.T.C. Gain on Investment	400	
		1,200
Total Income		25,495
Rounded off to Rs. 25,500		

Note : No tax as PFAOP's income does not exceed Rs. 40,000.

Allocation Amongst Partners

	A Rs.	B Rs.	C Rs.
Interest on Capital	300	400	800
Salary to B	—	6,000	—
Share of income in the Profit sharing ratio	7,198	7,198	3,599
Share out of P.F.A.O.P.'s income	7,498	13,598	4,399

Note: (*i*) Amount paid to a retiring partner is not a business expenditure, so disallowed.

(*ii*) Profit on sale of investment is considered to be a long-term capital gain.

Illustration 9. A, B, C and D were partners in a firm assessed as AOP sharing profits and losses in the ratio of 30 per cent, 25 per cent, 25 per cent and 20 per cent respecively. After six months D left the firm and E was taken in and profit sharing ratios were readjusted as follows :

A 25 per cent, B 25 per cent, C 25 per cent and E 25 per cent. The profit of the firm for the previous year amounted to Rs. 1,21,098 which included Rs. 7,500

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as interest on securities and interest of Rs. 3,000 charged to B on his drawings. This profit has been arrived at after debiting the following:

(*i*) Interest paid to B on his capial account Rs. 7,000.
(*ii*) Salary paid to C and D Rs. 1,200 and Rs. 6,000 respectively.
(*iii*) Rent of Rs. 6,000 paid to D.
(*iv*) Commission of Rs. 2,400 paid to E.
(*v*) Donations of Rs. 6,600.

Compute the total income of the PFAOP and allocate the same amongst the partners. Compute its tax liability, if total income of one of its partners is Rs. 69,000.

Solution

Computation of PFAOP's business income

			Rs.
Profit as per given in the Profit and Loss Account			1,21,098
Add: Disallowed items:			
Interest on capital	7,000		
Less: Interest on drawings	3,000		
		4,000	
Salary of Partners			
C	1,200		
D	6,000		
		7,200	
Commission to E		2,400	
Donation and charities		6,600	
			20,200
			1,41,298
Less: Income to be treated under a separte head of income			7,500
PFAOP's Business Income			1,33,798

PFAOP's Total Income	Rs.
P. & G.: Business Income	1,33,798
Other sources: Interest on Securities	7,500
	1,41,298

Deduction:	
Deduction of donations under section 80G	
Donations = 6,600	
Q.A. = 6,600 (Being less than 10% of G.T.I.)	
50% of Q.A. of Rs. 6,600	3,300
Total Income	1,37,998
PFAOP's tax on total income of Rs. 1,38,000	
At Maximum Marginal Rate *i.e.* 40%	55,200
[as one of its partner's income exceeds exempted limit]	

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Allocation amongst Partners

Pre-change *i.e.* First six months

	A	B	C	D
Interest on Capital	Rs.	Rs.	Rs.	Rs.
(7,000 – 3,000) × 1/2)	—	2,000	—	—
(6 months)				
Salary (6 months)	—	—	600	6,000
Share of Profit (6 : 5 : 5 : 4)				
[(1,37,998 × 1/2) (–) 8,600]	18,120	15,100	15,100	12,079
	18,120	17,100	15,700	18,079

Post-change *i.e.* last 6 months

				E
				Rs.
Interest on Capital	—	2,000	—	—
Salary	—	—	600	—
Commission	—	—	—	2,400
Share of Profit:				
[1,37,998 × 1/2) – 5,000]	16,000	16,000	16,000	15,999
	34,120	35,100	32,300	18,399

Note: Share of partners shall not be added in their individual income as PFAOP has paid tax at Maximum Marginal Rate *i.e.* 40%.

Illustration 10. XYZ, is a partnership firm assessed as AOP with X, Y and Z as partners sharing profits and losses equally. Z being the wife of X, carries on the business of Commission Agent. For the previous year ended 31st March, 1997 the Profit and Loss Account of the firm discloses a net profit of Rs. 2,00,000. The following particulars and informations are available on examination of the Books and Records:

(*i*) Z became a partner by investing capital from her own resources, her husband having contributed no part of it directly or indirectly. She is actively engaged in the business.

(*ii*) Salary of Rs. 6,000 was paid to Y.

(*iii*) Interest of Rs. 2,400 and Rs. 2,000 was paid to X and Z on their respective capital.

(*iv*) Z's godown was rented by the firm for which rent of Rs. 3,000 was paid to her.

(*v*) Tax of Rs. 10,000 paid during the year by the firm on a non-resident principal's account for whom it was treated as agent was written off as it become irrecoverable. The firm claims it either as an item of expenditure or as a bad debt.

The amounts noted in items (*ii*), (*iii*), (*iv*) and (*v*) above were debited to the Profit and Loss Account.

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X has no other source of income. Y has a further income of Rs. 2,000 from dividends. Z's only other source of income is the godown let out to the firm, the assessable income where from for the year is Rs. 2,000.
Determine:

(*a*) The total income of PFAOP.
(*b*) The allocation of the PFAOP's profit amongst the partners; and
(*c*) The gross total income of each partner.

State reasons for your treatment of each item of information given above.
(C.U., M.Com.)

Solution

Computation of PFAOP's income

		Rs.
Profit as shown in the Profit and Loss Account		2,00,000
Add: Disallowed items:	Rs.	
Salary to partner Y	6,000	
Interest on capital		
X	2,400	
Z	2,000	
Tax paid as agent of non-resident principal	10,000	
		20,400
PFAOP's business income being PFAOP's Total Income		2,20,400

PFAOP's Tax on Total income of Rs. 2,20,400 : It will pay tax at the rates applicable to an individual as total income of each partner (before including share from PFAOP) does not exceed the exempted limit *i.e.* Rs. 40,000

	Rs.
On Rs. 1,20,000	21,000
On Balance Rs. 1,00,400 40%	40,160
Tax Payable	61,160

Allocation of PFAOP's Income

	X Rs.	Y Rs.	Z Rs.
Salary	—	6,000	—
Interest on Capital	2,400	—	2,000
Share of PFAOP's income in the Profit-sharing ratio	70,000	70,000	70,000
Share out of PFAOP's income	72,400	76,000	72,000

Partner's Gross Total Income :

	Rs.
(1) X:	
Share from PFAOP	72,400
other incomes	NIL
Gross Total Income	72,400

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	Rs.
(2) Y:	
Dividends income	2,000
Share of PFAOP's Income	76,000
Gross Total Income	78,000
(3) Z:	
Income from house property (calculated)	2,000
Share of PFAOP income	72,000
Gross Total Income	74,000

Note 1. Partners can claim rebate of tax at average rate on share from PFAOP.
2. Rent paid to partner Z for using his building is an allowable deduction.

Q. No. 1 Partnership firm assessed as Firm (PFAF)

A and B are active partners and C and D are sleeping partners in a PFAF. A profit and loss account, drawn for the year ending 31-3-97 shows a profit of Rs. 25,000. The profit has been arrived at after allowing salary and interest to partners as follows :

	A	B	C	D
Salary	25,000	23,000	—	—
Interest @ 15%	2,000	4,000	6,000	3,000

Further the long term capital gains of the firm are Rs. 40,000. Partners shares the profit or loss equally. Compute the total income of the firm and its tax liability of interest to all partners and salary to active partners has been paid as per deed.

[Algappa University MCS Degree, August 1995]

[**Hints :** Book Profit Rs. 73,000; Allowable remuneration u/s 40 (b) Rs. 48,000 Total Income Rs. 65,000; PFAF's Tax Rs. 22,000]

Q. No. 2

XYZ is a firm assessed as firm consisting of three partners X, Y and Z. X and Y are partners in their capacity as kartas of their respective hindu undivided families. Mrs. X had invested Rs. 20,000 out of her own money in the firm. For the previous year 1996-97 the Assessing Officer wants to disallow interest of Rs. 3,600 paid by the firm to Mrs. X on the ground that Mrs. X, being a member of X's HUF (which is represented by X in the firm) is a partner in the firm and as a consequence interest paid to her is disallowable under section 40(b). Is he legally justified ? *[Company Secretary Inter Dec. 1991]*

[**Hints :** Mrs. X is creditor not partner. Hence Assessing Officer is not justified]

Q. No. 3

Profit and Loss Account of ABC and Co. (a firm of chartered accountants) for the year ending 31-3-97 is as follows :

	Rs.		Rs.
Expenses	10,000	Receipts from Clients	1,35,000
Depreciation	75,000	Dividend from Companies	25,000

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Remuneration to Working Partners	80,000	Net Loss	30,000
Interest on Capital to partners @ 20%	25,000		
	1,90,000		1,90,000

Other informations :

(*i*) Out of expenses of Rs. 10,000 Rs. 6,400 is not deductible by virtue of section 36 and 37.

(*ii*) Depreciation as per section 32 is Rs. 27,500.

Find out the amount of net income of the firm for the assessment year 1997-98. The remuneration and interest on capital to partners have been paid according to partnership deed which was submitted alongwith return.

[*Company Secretaries Final Dec. 1993*]

[**Hints :** Allowable remuneration Rs. 73,260 professional Gain Rs. 8,140; Total Income Rs. 33,140] [P-8]

Q. No. 4

From the information given below find out the amount of remuneration which can be debited to P & L A/c of the firm and how much income of partners shall be changeable to tax under the head profits & Gains :

	Rs.
Book Profit (after debiting the following)	40,000
Following payments have been made as per partnership deed which had been submitted alongwith return for the assessment year 1994-95 :	
salary to X (working partner)	84,000
salary to Y (non-working partner)	20,000
Commission to Z (working partner)	60,000
Interest on Capital to partners @ 24%	
To X	12,000
To Y	9,000
To Z	6,000

[**Hints:** Book Profit Rs. 2,10,750, Limit on remuneration paid to Mr. X and Mr. Z—allowed Rs. 1,36,800. Partner X's individual income Rs. 88,800, Y's individual income Rs. 6,750, Z's individual income Rs. 61,500] [P-1]

Q. No. 5

Shri A and B are equal partners in a firm, whose Profit and Loss Account for the year ended 31st March, 1997 is given below and has submitted its partnership deed along with return. The payment of salary, commission and interest @ 12% has been made as per deed.

	Rs.		Rs.
To Salary, Wages and Bonus	4,000	By Gross Profit	44,500
,, General Expenses	6,000	,, Interest (Bank)	1,000
,, Sales Tax	300	,, Bad Debts recovered (Disallowed in earlier year's assessment)	1,100
,, Rent, Rates and Taxes	2,500		
,, Income Tax Reserve	1,500		

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,, Depreciation on old plant and machinery		1,200		
,, Bad Debts written off		300		
,, Bad Debts Reserve		800		
,, Advertising		2,000		
,, Subscription		1,000		
,, Donations to a Hospital		1,000		
,, Loss on sale of motor car		9,000		
" Interest on capital :				
	Rs.			
A	1,500			
B	1,500			
		3,000		
,, Partner's salaries :				
A ,,	1,200			
B ,,	1,800			
		3,000		
,, Commission to B		1,000		
,, Net Profit :				
A ,,	5,000			
B ,,	5,000			
		10,000		
Total		46,600	Total	46,600

Notes: (*a*) General expenses include Rs. 200 being legal charges for drawing up a new partnership deed.

(*b*) Advertising represents Rs. 2,000, being cost of insertion in trade journals.

(*c*) The motor car is entirely used for private purpose of the partners.

(*i*) The written down value of old plant and machinery as on 1st April, comes to Rs. 10,000.

(*ii*) On 1-7-1996 a new plant and machinery (complete unit) amounting to Rs. 10,000 was purchased & installed and put into use for commercial production.

(*iii*) Depreciation at 25% per cent is allowable on all plant & machinery.

(*d*) Rent, Rates and Taxes include Rs. 1,200 being rent paid to A for premises used for business.

Compute the assessable income of the firm and find out partners' income taxable under the head Profits & Gains.

[**Hints :** Business income Rs. 16,600; Total Income Rs. 17,100; Depreciation on P and M Rs. 5,000; A's income under P & G 2,700 B's income under P & G 4,300.] [P-4]

Q. No. 6

A partnership with A, B and C as equal partners submits the following details for the assessment year 1997-98 :

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(*a*) Profit from business (after deducting the following amounts)	Rs.	Rs.	Rs. 81,000
Salary to A		90,000	
Salary to B		60,000	
Interest on Capital @ 20%			
A	5,000		
B	4,000		
C	3,000		
		12,000	
Donations to N.D.F.		2,000	
(*b*) Interest on Securities (Gross)			9,000
(*c*) Income from property (Computed)			14,000
(*d*) Dividends (Gross)			500
Other incomes of the partners are as given below :			
A Income from speculation			10,000
Property Income (Computed)			10,000
C Profit from an A.O.P.			20,000
Speculation loss			50,000

Compute firms total income. Firm has submitted the certified copy of its partnership deed along with its return. According to this deed *interest* as per above and salary of Rs. 90,000 and Rs. 60,000 is to be paid to working partners A and B respectively. Compute the total income of partners.

[**Hints** : Firms total income Rs. 1,10,520 after allowing remuneration of 1,46,180 to partners u/s 40(b) A's total income Rs. 1,12,208 B's total income Rs. 62,072 C's total income Rs. 22,700 share from firm exempted] [P-6]

Q. No. 7

The Doctors, Dr. Ahalya Dr. Somanath are running a nursing home under a partnership firm sharing profits and losses equally and showed Rs. 16,600 as profit for 1996-97 after taking into account the following items:

Debits	
Operation charges to Dr. Somanath (Rs. 100 per operation)	1,500
Remuneration to Dr. Ahalya	6,200
Honorarium to Dr. Somanath	3,000
Bonus to *each* Doctor	2,000
Donation to Janata Party	5,000
Interest on Capital to each Doctor @ 15% P.A.	2,000
Purchase of surgical equipment	12,500
Credits :	
House property rent	9,600
Dividend on shares (Gross)	4,000

Compute firm's total income and find out the income of the partners taxable under the head Profits & Gain :

Firm's deed (certified copy submitted) provides for payment of operation charges, honorarium remuneration, bonus and interest on capital.

[**Hints** : Professional Income Rs. 17,375; House Property Rs. 7,680 Other Sources Rs. 4,000; Total Income Rs. 29,055. Dr. Ahalya's professional gain Rs. 10,200 and Dr. Somanath's professional gain 8,500] [P-2]

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Q. No. 8

A, B, C, and D are partners having equal shares in a partnership firm. Having been in financial difficulties, they admitted a minor X to the Rs. benefits of partnership from 1-4-1996. The minor contributed capital of Rs. 1,25,000 and he was given a share of 25 paise in a rupee of the profits. The Profit and Loss account of the firm for the year ending 31-3-1997 shows the following :—

	Rs.		Rs.
Salaries	60,000	Gross Profit	2,50,450
Rent	20,000	Bad debts recovered	15,000
Insurance charges	12,000		
Travelling Exps.	15,000		
Legal charges	6,000		
Interest payable	48,000		
General charges	14,000		
Income tax paid on employees salary	6,000		
Charity	4,000		
Net Profit	80,450		
	2,65,450		2,65,450

(*a*) Salaries include Rs. 2,000 p.m. to partner A who looks after the firm.

(*b*) Rent include Rs. 500 per month for the rent of godown belonging to partner B.

(*c*) Interest charges include Rs. 30,000 as interest on the capital of X. @ 24% was credited to his account on 30.3.97.

(*d*) Legal charges include Rs. 2,000 paid for drafting of partnership deed.

(*e*) General expenses include car expenses of Rs. 250 p.m. to partner C for going out on firm's business. Rs. 1,000 for the cost of a new typewriter and Rs. 3,000 for putting up a partition in the office.

(*f*) Bad Debts recovered in the previous year were not allowed by the A.O. when they became bad.

The firm has submitted certified copy of its deed. Salary to partner A, who is working partner and interest to minor partner X has been paid in accordance with deed. Compute firm's business income and partners income taxable under the head Profits & Gains. *[Adapted B.Com P.U. April 1993]*

[**Hints :** Business Profit Rs. 79,700. PFAF's tax Rs. 31,880 A's Business income Rs. 24,000 B's business income NIL HP Rs. 4,800 C's income Nil, Minor partner X's income Rs. 22,500 to be clubbed with parents income u/s 64(IA) [P-3].

Q. No. 9

From the profit and loss account of Mishra Traders, a partnership firm, for the year ending 31st March compute taxable income for the assessment year 1997-98.

Profit and Loss Account

	Rs.		Rs.
To Salaries	36,000	By Gross Profit	96,000
" Rent	12,000	" Commission	5,000
" Electricity and Water	2,200	" Scrap Sales	5,000

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"	Rent, Rates and Taxes	2,500	"	Refunds Received on Excise Penalty	2,500
"	Motor Car Expenses	9,000	"	Income-tax	7,700
"	Entertainment Expenses	3,000	"	Surplus on Sale of Shares	15,000
"	Repairs	6,000			
"	Depreciation	8,000			
"	Trade Expenses	6,500			
"	Legal Expenses	3,500			
"	Net Profit	42,500			
		1,31,200			1,31,200

Other Particulars

(*a*) Salaries included Rs. 12,000 paid to managing partner X.

(*b*) Rent include Rs. 6,000 paid to a partner for the premises occupied by the firm.

(*c*) Rent, rates and taxes include municipal taxes of Rs. 1,000 paid on the premises of the partner, to be borne by him.

(*d*) Motor car expenses included Rs. 3,600 conveyance allowance paid to managing partner. He claims to have spent whole of such amount in performance of his duties.

(*e*) Repairs include cost of electric motors replaced at a cost of Rs. 3,000 each.

(*f*) Trade Expenses include :

(*i*) Donation to Charitable Institution Rs. 1,500

(*ii*) Diwali Pooja Expenses Rs. 1,000

(*g*) Legal Expenses include Rs. 500 paid to advocate in connection with the litigation of the partner's property;

(*h*) Excise penalty was disallowed when debited in the earlier year, *i.e.*, assessement year, 1995-96.

(*i*) Shares sold were held by the firm for more than 12 months.

The firm has submitted its instrument of partnership which provides for salary paid to managing partner X.

[**Hints :** Salary and conveyance allowance allowed u/s 40 (b); Excise penalty recovered is exempted. Dep. on electric motors Rs. 1,500 Firm's business income Rs. 24,800 and total income Rs. 39,050 PFAF's tax Rs. 14,120] [P-9]

Q. No. 10

A firm which consists of P, Q, R as partners has submitted its authenticated copy of partnership deed to the Assessing Officer alongwith its return submits following information.

A. Net Profit Rs. 90,000 after debiting the following :

Salary to P	Rs. 1,20,000
Salary to Q	Rs. 60,000
Interest on Capital @ 19%	
to P	Rs. 19,000
to Q	Rs. 9,500
to R	Rs. 7,600

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Donation to National Foundation for Communal Harmony — Rs. 4,000
B. Interest on Govt. Securities — Rs. 15,000
C. Income from House Property (Computed) — Rs. 24,000
D. Dividend from tea Company — Rs. 6,000

Compute firm's total income if the instrument of partnership provides for payment of Salary to P Rs. 1,20,000 and Q Rs. 60,000. Also compute partner's income taxable under the head Profits and Gains.

[**Hints :** Allowable remuneration Rs. 1,76,540; Deduction u/s 80 G Rs. 4,000 Total Income Rs. 1,74,560 Firm's Tax Rs. 69,824. P's Income Rs. 1,17,693, Q's Income Rs. 58,847] [P-1/0]

Q. No. 11

R and N are partners in a firm from the following P & L account compute the amount of book profits of the firm and determine total income of the firm. Also compute the income of partners taxable under the head Profits and Gains.

	Rs.		Rs.
General Expenses	20,000	Gross Profit	2,10,000
Salaries to staff	30,000	Rent from	
Bonus to employees	6,000	House Property	36,000
Depreciation	10,000	Dividend (gross)	22,000
Bad debts	2,500	Interest on deposits with	
Excise duty	10,000	Panjab Urban Deve-	
Reserve for Bad Debts	3,000	lopment Authority	5,000
Donation to J.N.M. Fund	3,000		
Repairs to House Property	1,500		
Insurance of			
House property	500		
Charities	1,500		
Remuneration to Partners			
R 1,00,000			
N 10,000			
	1,10,000		
Interest on Capital			
R 12,000			
N 10,000	22,000		
Net profit	53,000		
	2,73,000		2,73,000

Additional Information

1. Staff Salaries include Rs. 3,000 paid to a gardener working at the residence of R
2. R is a working partner
3. Interest on Capital has been paid at 20% p.a.
4. Depreciation allowable under I.T. Rules is Rs. 10,500.

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The firm had submitted its instrument of partnership alongwith return for the assessment year 1997-98. Remuneration to R and interest on capital have been paid according to partnership deed.

[**Hints :** Firm's Book Profit Rs. 1,08,200; Allowable remuneration Rs. 87,420; Firm's total income [P & G Rs. 20,780; HP Rs. 28,300 + Other Sources Rs. 27,000 Deduction u/s 80G Rs. 1,500] Rs. 74,580; R's income under P & G (Rs. 87,420 + Rs. 10,800) Rs. 98,220 and N's income under P & G Rs. 9,000] [P-11]

Q. No. 12

The profit and loss Account of the firm ABC shows a balance of Rs. 15,000(+). The firm has three partners A, B and C sharing profits and losses in the ratio of 7 : 5 : 3. From this P. and L. A/c following information is obtained.

(*i*) Closing stocks of goods have been valued year after year at 10% below cost, the values on 31.3.96 and 31.3.97 being Rs. 1,12,000 and Rs. 94,000 respectively.

(*ii*) The debits to the profits and loss account includes salaries to A, B and C Rs. 6,000 and Rs. 9,000 and Rs. 12,000 respectively, and interest @ 15% of Rs. 4,000 and Rs. 2,000 to A and B respectively. Partner A is working partner and his salary and interest to A & B is paid as per deed.

(*iii*) Depreciation debited to the accounts was Rs. 27,000 but the amount actually admissible for income-tax purposes is Rs. 25,000. A, B and C have separate sources of income also, and for the current year these sources show the assessable results for A, B and C at (+) Rs. 25,000, (–) Rs. 8,000 and (+) Rs. 2,000 respectively.

Compute the total income of the firm.

[**Hints :** Difference due to under debiting of stock; Rs. 2,000 Allowable remuneration Rs. 6,000; Interest fully allowed Firm's Business profit Rs. 36,000] [P-7]

Q. No. 13

The total income of M/s MSA and Co., a firm, was Rs. 2 lakhs before charging the following :

	Rs.
Salary to Partner M	48,000
to partner S	24,000
Commission to A	32,000
Interest @ 20%	
to M	20,000
to S	16,000

The partnership deed (whose certified copy has been submitted alongwith return) provides for payment of salary and commission to partners M, S and A who are working partners. Interest @ 20% has also been included in the deed.

Calculate firm's business income and partner's income taxable under head Profits and Gains.

[**Hints :** Allowable remuneration u/s 40 (b) Rs. 1,04,000 allowed interest @ 18% Rs. 32,400; Partner M's income under Profits & Gains Rs. 66,000; S's income Rs. 38,400 and A's income Rs. 32,000] [P-5]

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PARTNERSHIP FIRMS ASSESSED AS A.O.P. (PFAOP)

Q. No. 14

Asim, John and Rahim are Partners in a firm assessed as an AOP sharing profits and losses in the ratio of 5 : 3 : 2. Profit and loss account for the year ending on 31.3.1997 was as follows :—

Profit and loss Account

	Rs.		Rs.
To rent and taxes	6,000	By Gross Profit	40,000
To salaries	9,000	By Interest on securities	3,000
To Electric Charges	1,200		
To Interest on capital			
Asim	2,000		
John	1,500		
Rahim	1,000		
To Depreciation	2,500		
To Reserve for bad debt	500		
To Interest on Loan from John	300		
To commission to Rahim	1,000		
To Balance: Asim	9,000		
John	5,400		
Rahim	3,600		
	43,000		43,000

Notes : (*a*) Salary includes Rs. 2,000 paid to Rahim.

(*b*) Depreciation allowable amounts to Rs. 2,400.

Compute the **business income** of firm and show allocation of **business profit** amongst partners. *(Adapted Calcutta Univ., B.Com. Hons. 1980)*

[**Hints:** Firm's Business Income 23,400; Asim's share Rs. 9,800, John's share 6,480 and Rahim's share Rs.7,120] [P-13]

Q. No. 15

The total income of a firm assessed as AOP, ABC in which A, B and C are partners, share profits and losses in the ratio of 1 : 2 : 2 was assessed at Rs. 16,000. In computing the total income of Rs. 16,000 the Income-tax Officer has made the necessary adjustments in respect of the following sums:

Salaries of Rs. 12,000 and Rs. 8,000 to A and B respectively.

Interest of Rs. 1,000, Rs. 6,000 and Rs. 25,000 to A, B and C respectively.

Commission of Rs. 2,000, Rs. 5,000 and Rs. 7,000 to A, B and C respectively.

C has borrowed capital for his investment in the firm and had paid interest of Rs. 15,000 separately to the lender. Compute the share of the respective partners for their individual assessment. *[C.U., B.Com. (Hons.)]*

[**Hints:** A's share of Income from firm Rs. 5,000 B's share Rs. (–) 1,000 and C's share Rs. 12,000 C's total loss Rs. (–) 3,000] [P-21]

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Q. No. 16

PQR & Co., partnership firm assessed as AOP with three partners P,. Q and R sharing profits or losses in the ratio of 3 : 2 : 1, gives the following particulars of its Profits and Loss Account for the year ending on 31st March, 1997:

(*a*) Profit as per Profit and Loss Account Rs. 50,000.
(*b*) Investment Deposit Account debited to P & L A/c Rs. 40,000.
(*c*) Depreciation debited Rs. 75,000. Actually admissible Rs. 90,000.
(*d*) Entertainment expenses Rs. 10,000.
(*e*) Bad debts recovered and credited to Profit and Loss A/c— Rs. 15,000. This is recovery out of a debt of Rs. 40,000 written off as bad in 1994-95 of which only Rs. 30,000 was allowed in the relevant assessment.
(*f*) Salaries paid to Q Rs. 12,000
(*g*) Commission paid to R Rs. 20,000

Compute the total income of the firm and allocate the income amongst the partners. Each item of information above should be fully dealt within your answer.

[*C.U., B.Com., (Hons.)*]

[**Hints:** Firm's Total Income Rs. 97,000. P's share Rs. 32,500, Q's share Rs. 33,667, R's share Rs. 30,833] [P-20]

Q. No. 17

Anita, Beena and Chitra are partners in a firm assessed as AOP sharing profits and losses equally. Their capitals were:

Anita	Rs. 20,000
Beena	Rs. 30,000
Chitra	Rs. 10,000

The Profit and Loss Account of the firm for the Previous year ended 31st March 1997 showed a net profit of Rs. 10,000 after charging the following items:

1. Salary to Anita Rs. 300 per month and to Chitra Rs. 500 per month.
2. Interest on Capital at 6% per annum.
3. Rent to Anita Rs. 150 per month in whose building business was carried on.
4. Interest on loan taken from Beena Rs. 500.

Compute the total income of the firm and allocate it amongst the partners.

(*Mysore, B.Com.*)

[**Hints :** Firm's Total Income Rs. 23,700: Anita's share Rs. 8,133, Beena's share Rs. 5,633 and Chitra's share Rs. 9,934.] [P-26]

Q. No. 18

The Profit and Loss Account of Messrs Ram Gopal & Company for the year ending 31st March, 1997 is as follows:

Dr.	Rs.	Cr.	Rs.
To Salaries	5,000	By Gross Profit	78,000
To Salary to Partner R	3,000	By Interest on Fixed Deposits	2,000
To Commission to Partner G	2,000	By Dividend	1,000
To Shop rent paid to partner R	4,000		
To Income-tax	4,000		
To Presents	1,000		

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To Legal charges	2,000	
To Depreciation	8,000	
To Bad Debts	2,000	
To Net profit	50,000	
	81,000	81,000

You are required to ascertain the taxable income of M/s Ram Gopal & Co. a firm assessed as AOP and allocate it amongst partners R & G who share profits and losses equally

[**Hints:** Business Income Rs. 57,000; other sources Rs. 3,000 Total Income Rs. 60,000, R's share Rs. 30,500; G's share Rs. 29,500]. [P-27]

Q..No. 19

A, B and C are partners in a firm assessed as AOP sharing profits and losses equally. The net profit of the firm after deducting all expenses was Rs. 65,000 for the year ending 31st March 1997.

Compute the total income of the firm and the share of partners therein, if the expenses deducted in computing the above profits included the following items:

(*a*) Salary to B at Rs. 400 p.m.

(*b*) Rent to A, in whose building the business was being carried on at Rs. 200 p.m.

(*c*) Interest on: A's Capital Rs.2,750
B's Capital Rs.1,490
C's Capital Rs. 650

(*d*) Interest on Loan taken from A Rs. 700.

(*e*) Commission to C Rs. 4,300 (*M.Com. Nagpur*)

[**Hints:** Firm's Income 79,690; A's share Rs. 25,117; B's share Rs. 27,957 and C's share Rs. 26,616] [P-28]

Q. No. 20

Asha, Bindu and Chandrika are partners sharing profits and losses in the ratio of 2 : 2 : 1. The firm assessed as AOP's Profit and Loss Account for the year ended 31st March, 1997 showed a net loss of Rs. 40,000 after charging the following items:

	Rs.
Interest on capital:	
Asha	1,000
Bindu	2,000
Chandrika	3,000
Salary to Asha	3,000
Bonus to Asha	2,000
Bindu	2,000
Chandrika	2,000

Asha's taxable income from other sources was Rs. 25,000; while Bindu and Chandrika had no other sources of income.

Show how the assessment of a firm assessed as AOP and of the partners will be made. (*Mysore B.Com.*)

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[**Hints:** Firm's Loss Rs. 25,000: Firm to C/F whole of loss. Asha's Total Income Rs. 25,000] [P-16].

Q. No. 21

A a firm assessed as AOP whose accounting year is the financial year, had three partners P, Q and R at the beginning of the year sharing profits in the ratio of 2 : 2 : 1 respectively. R left partnership on Ist Dec. 1996 and was replaced by X who was an employee previously. The new profit sharing ratio is 3 : 3 : 2. The firm's accounts for 1996-97 show a profit of Rs. 84,000 after debiting Rs. 2,000 paid as interest to P ; Rs. 1,600 paid as interest to R ; Rs. 4,400 as rent for business premises to R ; Rs. 4,800 paid as salary to R at the rate of Rs. 600 per month and Rs. 3,600 paid as salary to X at the rate of Rs. 300 per month.

Compute PFAOP's total income and allocate it.

[**Hints:** PFAOP's business income Rs. 93,600; P's share Rs. 34,867 ; Q's share Rs. 32,867 ; R's share Rs. 17,333 ; X's share Rs. 8,533 and salary income (2,400—800 =1,600)] [P-7].

Q. No. 22

A, B and C are partners in a firm assessed as AOP sharing profits and losses in the ratio of 1/2, 1/4 and 1/4 respectively. After 8 months C left and D was taken in his place and the profit and loss sharing ratio was readjusted as follows:

A 6/16, B 5/16 and D 5/16

For the assessment year 1997-98 the accounts of the PFAOP disclosed a profit of Rs. 45,500 (including Rs. 2,000 realized as rent in respect of building having a municipal value of Rs. 3,000).

The above book profit had been worked out after debiting the following:

(*a*) Rs. 4,000 interest paid to A ;

(*b*) Rs. 6,000 salary paid to B ;

(*c*) Rs. 3,000 shop rent paid to C ;

(*d*) Rs. 1,500 commission paid to D.

The firm has to be allowed depreciation Rs. 15,000. The allowance has not been taken into account while calculating the above profit.

Compute the total income of the PFAOP and allocate it amongst the partners. [*B.H.U., M.Com.*]

[**Hints:** Firm's Business Income Rs. 40,000 ; House property Income Rs. 2,400 ; Total Income Rs. 42,400 ; A's share Rs. 18,288, B's share Rs. 14,306, C's share Rs. 5,400 and D's share Rs. 4,406] [P-18]

Q. No. 23

Arun and Barun were partners in a firm assessed as AOP whose accounting year ends on 31st March every year. On 1st April 1996 Shanti (Barun's wife) joined the PFAOP as a partner and thereafter all the three partners are entitled to share profits and losses equally. Shanti invested a sum of Rs. 2,00,000 as her capital in the firm, the sources of such investment being the gift received from her father. The other two partners have no capital in the PFAOP. Shanti is actively engaged in the business.

For the assessment year 1997-98, the firm's total income has been determined by the Income-tax Officer at Rs. 45,000 after making due adjustments in respect of the following items :

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(1) Salary :			
Arun		Rs. 15,000	
Barun		Rs. 10,000	
Shanti		Rs. 10,000	Rs. 35,000
(2) Interest on Capital :			
Shanti			Rs. 28,000
(3) Brokerage :			
Arun		Rs. 12,000	
Shanti		Rs. 12,000	Rs. 24,000
(4) Rent :			
Barun			Rs. 9,000

(for the office premises owned by him)

Arun won a prize of Rs. 10,000 in West Bengal State Lottery and a sum of Rs. 4,000 was deducted at source out of the same. Shanti holds 10,000 Equity shares of a company on which a dividend of 95 paise per share (subject to deduction of tax at source) was declared by the company in its Annual General Meeting held on 28th March, 1997. Apart from the above, no partner has any other income whatsoever.

Compute the total income of each of the partners and indicate the amounts on which they would be liable to tax respectively.

[I.C.W.A. Final Exam., New Syllabus]

[**Hints** : Arun's Total Income Rs. 18,000, Barun's Total Income Rs. 7,200, Shanti's Total Income Rs. 36,000] [P-9]

Q. No. 24

The profit and loss account of a PFAOP in which the partners X, Y and Z share profits and losses in the ratio 5 : 4 : 1 respectively discloses profit of Rs. 80,625 for the accounting year ending 31st March, 1997. Its profit was arrived at after the following debits and credits :—

Debits	Rs.	*Credits*	Rs.
Donation to National Defence Fund	11,000	Capital gain on sale of Scrap machinery	5,000
Speculation Losses	30,000	Dividend after deduction of tax at source Rs. 5,000	20,000
Salary to Partners :		Interest on Securities (Gross)	3,500
X Rs. 5,000			
Y Rs. 9,000			
Z Rs. 12,000			
	26,000		
Commission to X	6,000		
Office Rent (Paid to Y)	12,000		

Compute the total income of the PFAOP and show its allocation amongst the partners for the assessment year 1997-98.

[**Hints** : PFAOP's Business income Rs. 1,25,125; Total income Rs. 1,53,125; X's share Rs. 71,563, Y's share Rs. 57,450 Z's share Rs. 24,112] [P-23]

Q. No. 25

PFAOP with A, B and C as equal partners submits the following details for the previous year ending on 31.3.97.

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1. Profits from business after following deduction : Rs. 81,000

		Rs.
(*a*) Salary to A		9,000
(*b*) Penal interest paid for non-payment of income-tax to the Govt.		5,000
(*c*) Interest on capital	A	5,000
	B	4,000
	C	3,000
(*d*) Donation to National Defence Fund		2,000
		28,000

2. Interest on Securities (gross) 9,000
3. Income from House Property (computed) 15,000
4. Dividends on preference shares (gross) 600

Compute the total income of the PFAOP and show how the income will be allocated amongst the partners.

[**Hints :** Profits & Gains Rs. 1,09,000; House Property Rs. 15,000 Other sources Rs. 9,600 Deduction u/s 80 G Rs. 1,000 Total income Rs. 1,32,600 A's share Rs. 51,200, B's share Rs. 41,200 and C's share Rs. 40,200] [P-15]

Q. No. 26

ABC & Co. is an A.O.P . with A, B and C as members who share profits and losses in the ratio of 2 : 3 : 5.

The P. & L. A/c of the AOP for the year ended 31st March, 1997 disclosed a net profit of Rs. 1,20,000. The net profit was arrived at after deducting the following :

(*a*) Salary to A Rs. 18,000;
(*b*) Interest to B Rs. 6,000; and
(*c*) Rent to C Rs. 9,000.

Compute the Taxable Income of the AOP and allocate it amongst members.

[**Hints :** Total income Rs. 1,44,000 A's share Rs. 42,000 B's share Rs. 42,000 and C's share Rs. 60,000] [P-12]

Q. No. 27

A and B are partners in a PFAOP sharing profit and loss in the ratio of 2 : 1. The following is the Profit and Loss Account :

		Rs.		Rs.
To Sundry Expenses		20,800	By Gross Profit	55,620
" Charity		570	" Commission	600
" Bad debts reserve		1,430		
" Legal charges		2,860		
" Interest on capital :				
A	1,280			
B	750	2,030		
" Profit :				
A	19,020			
B	9,510			
		28,530		
		56,220		56,220

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The items of sundry expenses include salary of A, Rs. 1,800 and that of B, Rs. 1,200. It also includes Rs. 1,500 in respect of the rent of residential house of the two partners. The house is shared half and half according to the terms of the agreement.

Depreciation on plant and machinery which is calculated at Rs. 3,340 has not been provided for in the above Profit and Loss Account.

Other incomes (computed under Income-tax Act) of the partners are :

	Rs. A	Rs. B
Interest on Govt. Securities	400	2,100
Income from property	600	—
Interest on P.O. Saving Account	—	30
	1,000	2,130

Your are required to determine the total income of the PFAOP and that of its partners individually.

[Hints : Total income Rs. 33,720; A's share Rs. 22,207; B's share Rs. 11,513 A's total income Rs. 22,807 B's total income Rs. 11,513] [P-22]

Q. No. 28

Your are given the Profit and Loss Account of XYZ & Co., an AOP. You are required to compute total income of the AOP for income-tax purposes and allocate the same amongst members for the year ending 31st March, 1997 :

XYZ & Co.

	Rs.	Rs.		Rs.	Rs.
To Partner's Salaries :			By Gross Profit		10,000
X	8,000		" Interest on Drawings :		
Y	4,000		X	1,000	
Z	2,000		Y	600	
		14,000	Z	400	
					2,000
To Interest on Capital :			By Loss trsns-ferred to Capital Account :		
X	3,000		X	3,000	
Y	2,000		Y	3,000	
Z	1,000		Z	3,000	
		6,000			
To Commission to X		1,000			9,000
Total		21,000	Total		21,000

[B.Com., Panjab]

[Hints : Total income Rs. 10,000; X's share Rs. 8,000 Y's share Rs. 2,400; Z's share (–) Rs. 400]

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Q. No. 29

Bengal Traders is a PFAOP with three partners. Sarvashri S.P. Sen. P. Mukherjee and R.C. Bhatt having their respective interest in the PFAOP in the ratio of 2 : 1 : 1. For the year ended 31st March, 1997 the PFAOP shows a net profit of Rs. 30,000.

The profit and loss account shows the following items of deductions :

(*i*) Salary paid to :
P. Mukherjee Rs. 3,600
R.C. Bhatt Rs. 4,800

(*ii*) Interest on Capital :
S.P. Sen Rs. 3,000
P. Mukherjee Rs. 2,000

(*iii*) Commission paid to :
P. Mukherjee Rs. 2,400
R.C. Bhatt Rs. 3,000

(*iv*) Customs penalty paid Rs. 1,500

(*v*) Rent paid Rs. 1,800 to Shri P. Mukherjee is respect of a godown let-out by him to the firm.

Compute the total Income of the PFAOP and show its allocation between the partners of the relevant assessment year indicating your reasons whenever necessary. *[C.U., B.Com. (Hons.)]*

[**Hints :** Total income Rs. 50,300; Sen's share. Rs. 18,750; Mukherjee's share Rs. 15,875 and Bhatt's shares Rs. 15,675] [P-25]

Q. No. 30

A, B and C are equal partners in a PFAOP carrying on Trading Business. The profit of the PFAOP for the year ending 31-3-1997 is Rs. 4,00,000 after adjusting the following :

(*i*) Salary of Rs. 1,000 p.m. to each of partners.

(*ii*) Commission of Rs. 30,000 to C.

(*iii*) Interest of Rs. 14,000 on a loan advanced by A to the PFAOP.

(*iv*) Income-tax paid Rs. 25,000 on behalf of foreign company for which the firm was assessed as an agent.

(*v*) Loss of Rs. 70,000 in speculation in shares.

(*vi*) Extension of factory building costing Rs. 50,000.

Compue the total income of the PFAOP, its tax and allocate the income amongst the partners.

Particulars of other incomes of partners are also available to compute the total income of each partner.

A had borrowed Rs. 1,00,000 @ 12% and have given the same to the firm as loan @ 14%. A's only other income Rs. 20,000 from another firm assessed as AOP as share of his income from that firm. B has a house property at Delhi which is let out at a rent of Rs. 2,000 p.m. Its market rental value being Rs. 30,000 p.a. The expenses incurred by 'B' in regard to this house are :

Municipal taxes @ 10% of rent received. Repairs Rs. 10,000.

Rs. 12,000 as interest paid on the mortgage of the house. The money of the mortgage was utilised for the renovation of house. He has also incurred collection charges of Rs. 3,000. The house remained vacant for 2 months.

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C's only other income is Rs. 1,00,000 from a State Lottery.

[**Hints :** Total income Rs. 6,20,000; tax Rs. 2,22,000 A's share Rs. 2,06,000 Total income Rs. 20,000; B's share Rs. 1,92,000 Total income Rs. 5,480; Partners C's share Rs. 2,22,000 Total income Rs. 95,000. Share from PFAOP is fully exempted as PFAOP has to pay tax at MMR] [P-25]

QUESTIONS

1. Define partnership firm,. When can a firm be assessed as firm ?
[B.Com. Hons. Delhi]
2. Discuss the provisions of Income-tax Act regarding computation of a firm's business income.
3. What are the restrictions imposed u/s 40(b) of the income-tax Act 1961 on remuneration and interest payable to partners of a firm ?
4. What are the provisions of Income-tax Act regarding the assessment of a partnership firm assessed as an association of persons ?
5. Distinguish between a firm assessed as firm and a firm assessed as an AOP.
[B.Com. GNDU]

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4 ASSESSMENT OF COMPANIES

What is company and its various types?—Computation of Gross total income of a company— Carry forward & set off of loss of companies— Deductions u/s 80,— Agricultural income of companies— Illustrations and Questions.

Company

Section 2 (31) includes a company within the definition of person. The 'Company' assessees have been contributing largest amount of revenue to the exchequer. The definition of the term 'Company' under the Income-tax Act is wider than in the Companies Act, 1956. Section 2 (17) defines a company as:

(*i*) any Indian Company; or

(*ii*) any body corporate incorporated by or under the laws of country outside India; or

(*iii*) any institution, association or body which was assessed under Income-tax Act, 1961 as a Company for any assessment year up to and including the assessment year 1970-71; or

(*iv*) any institution, association or body whether incorporated or not and whether Indian or non-Indian which is declared by general or special order of the Board to be a Company.

Under the provisions of clause (iv) even an association of persons or body of individuals whether incorporated or not may be taxed as Company under the orders of Central Board of Direct Taxes.

Indian Company

According to section 2 (26), Indian Company includes:

(*i*) a company formed and registered under any law relating to companies;

(*ii*) a corporation established by or under a Central, State or Provincial Act;

(*iii*) any institution, body or association declared as Company by the Board.

In all the above cases the principal office of the company, corporation, institution, association or body must be situated in India.

CLASSIFICATION OF COMPANIES

1. Companies in which public are substantially interested. A company is said to be a company in which public are substantially interested if:

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(*a*) It is a Company owned by the Central or State Government or the Reserve Bank of India or if at least 40% of its shares (by monetary value) are held (singly or jointly) by the Government or the Reserve Bank of India or a Corporation owned by that Bank; or

(*b*) It is a Company which is registered under sec. 25 of the company Act; or

(*c*) It is a Company having no share capital and if having regard to its objects the nature and compositions of its membership and of other relevant consideration it is declared by order of the Board to be a Company in which public are substantially interested.

Provided that such order shall hold good for only such assessment year or years as may be specified in the declaration; or

(*d*) It is a Company which is not a private Company as defined in the Companies Act, 1956, and the conditions specified either in A or in B are fulfilled;

A. Shares in the Company (not being shares entitled to a fixed rate of dividend) were as on the last day of relevant previous year listed in recognised stock exchanges of India.

B. (*i*) Its shares (not being shares entitled to a fixed rate of dividend) carrying not less than 50% of voting power (40% in case of Industrial Company) have been allocated unconditionally to or acquired unconditionally by and were held throughout the relevant previous year beneficially by:

(*a*) the Government; or

(*b*) a Corporation established by a Central, State, Provincial Act; or

(*c*) any Company in which public are substantially interested or its 100% subsidiary; or

(*d*) the public, not being a director, or a Company in which the public *are not* substantially interested;

(*ii*) The said shares were during the relevant previous year freely transferable by the holder to the other members of the public; and

(*iii*) the affairs of the Company or the shares carrying more than 50% of its total voting power were at no time during the relevant previous year controlled or held by five or less persons.

Explanation to Clause B (iii):

Following rules are to be observed while counting the number of five or less persons who may control or hold 50% of voting power:

(*a*) the Governments, Central or State, or a Statutory Corporation, or a Company in which public are substantially interested or a subsidiary company of such Company shall not be taken into account; and

(*b*) the persons who are relatives of one another and persons who are nominees of any other person together with that person shall be treated as single person.

2. Widely Held Company. A company in which the public are substanitally interested is known as widely held company.

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3. Closely Held Company. A company in which the public are not substantially interested is referred to as a closely held company.

4. Industrial Company. Means an Indian Company whose business consists wholly in the construction of ships or in the manufacture or processing of goods or in the mining or in the generation or distribution of electricity or any other form of power.

Provided that the income attributable to any or more of the aforesaid activities included in the total income of the previous year is not less than 51% of such total income.

5. Domestic Company. An Indian Company or any other company which, in respect of its income liable to income-tax under the Income-tax Act, 1961, for the assessment year commencing on 1st of April 1961 has made the prescribed arrangements for the declaration and payment of dividends payable out of such income under section 194 of the Act.

6. Foreign or Non-domestic Company. A company which is not a domestic company will be known as foreign company.

7. Investment Company. Investment company is a company whose gross total income consists mainly of income chargeable to tax under the heads 'Income from House Property', Capital Gains' and 'Income from Other Sources'. Section 109 (*ii*) (*i*)].

8. Consultancy Service Company. Means an Indian Company whose business consists wholly in the provisions of technical know-how or in rendering of services in connection with provision of technical know-how, to other persons.

9. Trading Company. It means a company whose business consists wholly or mainly in dealing with goods or merchandise manufactured, produced or processed by a person other than that company and whose income attributable to such business included in its gross total income is not less than 51% of the amount of such gross total income [Section 109 (*ii a*)].

10. Banking Company. Banking company means a company to which the Banking Regulation Act, 1949 applies and includes any Bank or banking institution referred to in Section 51 of that Act.

Residence of Company [Section 6 (3)]

Determination of total income of company and its liability depends upon the residential status of a company during the relevant previous year.

Under the provisions of Section 6(3), companies can be classified into two categories:

(*i*) Resident Companies, (*ii*) Non-resident Companies.

A company is said to be a *Resident Company* if (*a*) it is an Indian Company; or (*b*) during the relevant previous year, the control and management of its affairs is situated wholly in India.

All Indian companies essentially are 'Resident' in India even if the control and management of its affairs is situated outside India. Even a foreign company can be

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resident in India if the whole of the control and management of its affair is situated in India, *e.g.*, A company was carrying on its business in Nepal but the Board of Directors held its meetings in Delhi and Directors retained complete control of the business. Such a company will be 'Resident' in India for tax purposes. Any company which is not a resident company shall be non-resident company.

Computation of Gross Total Income of a Company

1. Headwise Calculation. Income of the company is to be computed headwise in same manner. Company cannot have income taxable under the head "Salaries." For computing the income from let out house property same rules have to be applied as are applicable in case of other assesses.

2. Computation of Business Profits. The method of calculation of taxable profits is same but some of the provisions given under this head are applicable only in case of companies. These are:

(a) Expenditure on Family Planning [Section 36 (ix)]

Only company assessees can debit any expenditure incurred on promotion of family planning amongst its employees. Revenue expenditure is fully allowed but capital expenditure can be debited in five equal instalments.

(b) Disallowance of certain expenses [Section 40]

(*i*) any expenditure which results into a benefit or amenity to a director or a person having substantial interest in the affairs if a company whether directly or indirectly, or to a relative of any of these persons;

(*ii*) Any expenditure incurred by company in respect of any assets of the company which are used by the director, or a person having substantial interest or any of their relatives for their personal benefit, shall be disallowed if A.O. feels that they are excessive or unreasonable.

3. Computation of Gains/Losses—in same manner

4. Set-off and Carry forward of capital losses

Both short-term and long-term are to be treated in same manner and losses relating to the period after 31-3-87 can be set off from Capital Gains income only of the same year. If still unadjusted, the amount so unadjusted can be carried forward for 8 succeeding previous years to be set off from income taxable under the head "Capital Gains".

In case long-term capital loss relates to a period prior to 1-4-87 and is being brought forward it shall be reduced by an amount calculated at the rates given u/s 48 (2) and balance shall be carried forward for a period not exceeding 4 previous years succeeding the previous year in which such loss was incurred.

5. Provisions relating to carry forward and set-off of accumulated loss and unabsorbed depreciation in certain cases of amalgamation (Section 72A).

In case a company owning an industrial undertaking amalgamates with another company, the accumulated loss and the unabsorbed depreciation of amalgamating company shall be deemed to be the loss or depreciation of the amalgamated company

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for the previous year in which amalgamation was effected and the other provisions of this Act relating to set-off and carry forward of loss and unabsorbed depreciation shall apply accordingly provided the following conditions are fulfilled:

(*i*) that the accumulated loss of the amalgamating company before amalgamation exceeds fifty per cent of the aggregate of its paid-up share capital;

(*ii*) that the amalgamating company was not, immediately before its amalgamation, financially viable;

(*iii*) that the amalgamation was in public interest;

(*iv*) that such other conditions as Central Government may notify in the Official Gazette to ensure that the benefit under this section would facilitate the rehabilitation or revival of the business of amalgamating company; and

(*v*) the Central Government makes declaration to this effect [Section 72 A (1)].

The benefit of set-off or carry forward shall not be available to the amalgamated company if it carries on the business of amalgamating company after making any modification or reorganisation and such modifications or reorganisation are not approved by prescribed authority. The amalgamated company shall have to furnish, alongwith return of income, a certificate from the specified authority to the effect that adequate steps have been taken by the company for the rehabilitation or revival of the business of the amalgamating company [Section 72 (2)].

The Finance Act 1978 has introducted sub-section (3) under which specified authority shall communicate to the amalgamating company about the fact that it is satisfied with the scheme submitted and it would make such recommendations to the Central Government after amalgamation is affected.

Accumulated Loss— means so much of loss of the amalgamating company under the head 'profits and gains of business or profession' (not being a loss sustained in a speculation business) which the amalgamating company would have been entitled to carry forward and set-off under the provisions of section 75, if the amalgamation had not been affected.

Unabsorbed Depreciation— means so much of the allowance or depreciation of the amalgamating company which remains to be allowed and which would have been allowed to the amalgamating company under the provision of the Act if the amalgamation had not been affected.

6. Carry forward and set-off Losses of Certain Companies
[Section 79]

Where change in shareholding has taken place in a previous year in the case of a company not being a company in which the public are substantially interested no loss incurred in any year prior to the previous year shall be carried forward and set-off against the income of the previous year unless:

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(*a*) On the last day of the previous year the shares of the company carrying not less than 51% of the voting power were beneficially held by persons who beneficially held shares of the company carrying not less than 51% of the voting power on the last day of the year or years in which the loss was incurred; or

(*b*) The Assessing Officer is satisfied that the change in the shareholding was not effected with a view to avoidance or reducing any liability of tax.

7. Deductions u/s 80

Company assessees are entitled to claim following deductions u/s 80 out of Gross total income:

(*i*) Donations [Section 80G]
(*ii*) Profit from Foreign contracts [Section HHB]
(*iii*) Profit from Exports [Section 80HHC]
(*iv*) Earning in convertible foreign exchange [Section 80HHD]
(*v*) Profit from export of software etc. [Section 80HHE]
(*vi*) New Tax holiday 80 I A
(*vii*) Royalty from foreign companies (Section 80 O)

For detailed treatment of these deductions, please refer to chapter "Deductions out of gross total income" in Part II of this book.

8. Agricultural Income of a Company

It is not to be integrated with non-agricultural income of the company. In case of a company engaged in tea plantation and tea processing industry, its 60% of income is agricultural income and 40% is business income.

PROVISIONS OF MINIMUM ALTERNATIVE TAX ON COMPANIES (MAT) [Section 115 JA]

1. These provisions are applicable on all those Indian companies whose total income as computed under this Act in respect of any previous year relevant to the assessment year commencing on or after 1.4.1997, is less than 30% of book profits.
2. For the purposes of levying tax on such companies total income as computed under Income-tax Act shall be disregarded and **30% of Book profit** shall be deemed as total income for such previous year.
3. Every such company shall prepare its profits and loss account in accordance with the provisions of part II and III of Schedule VI of the Companies Act 1956.
4. While preparing profit and loss account **depreciation will have to be the same as has been charged for preparing the accounts to be presented at the time of annual general meeting of the company.** In case the company has its accounting year which is different than financial year the amount of depreciation (as mentioned above) shall have to be adjusted.

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5. The term Book profit means the net profit as per profit and loss account which is to be increased by the following if these are debited or are not credited to P & L A/c :
   - (*a*) any amount of income-tax paid or payable and any provision for such tax,
   - (*b*) any amount carried to any reserve by whatever name called,
   - (*c*) any amount set aside to meet any liability other than ascertained liabilities,
   - (*d*) any amount set aside as provision for losses of subsidiary companies,
   - (*e*) any amount or amounts of dividend paid or proposed,
   - (*f*) any amount of expenditure relating to such incomes which do not form part of total income u/s 10 to 13.

Amount so arrived at shall be reduced by the following :

- (*i*) any amount withdrawn from reserves other than reserve specified u/s 80 HHD, or from provisions, if any such amount is credited to the P & L Account. Any amount withdrawn from a reserve created or provision made on or after 1.4.1997, the amount of said withdrawal shall not be deducted if such amount has not increased the book profits of such year.
- (*ii*) any income which is not to be included in total income as given u/s 10 to 13 but has been credited.
- (*iii*) any amount of loss brought forward or unabsorbed depreciation which ever is less, [B/F loss shall not include unabsorbed depreciation].
- (*iv*) any amount of profits derived by an undertaking from the business of generation and distribution of electricity.
- (*v*) any amount of profits derived by an undertaking set up in industrially backward districts as notified u/s 80IA during the period it is eligible for deduction u/s 80IA.
- (*vi*) any amount of profits derived by an undertaking set up in infra structural sector as notified u/s 80IA during the period it is eligible for deduction u/s 80IA.
- (*vii*) any amount of profits of a sick industrial company for the period from the assessment year in which the unit became industrially sick till the assessment year during which the entire net worth of the company equals or exceeds the accumulated losses.
- (*viii*) any amount of profits derived from the export of goods or merchandise to which section 80 HHC is applicable. **(This provision has been inserted with effect from 1998-99.)**

6. The provisions contained above shall not have any effect on unabsorbed.

TAX CREDIT IN RESPECT OF TAX PAID UNDER MAT [Section 115JAA]

1. In case any amount is paid u/s 115JA by a company for any assessment year, such company shall be allowed credit of amount of tax so paid in prescribed manner.

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2. The tax credit to be allowed shall be an amount equal to difference between the amount of tax paid u/s 115JA and tax payable on his total income as computed under this Act.
3. No interest shall be allowed on the amount of tax credit to be given.
4. Amount of tax credit as determined above shall be allowed to be carried forward upto 4 assessment years succeeding the assessment year in which such credit became due.
5. Tax credit will be allowed in the year in which tax becomes payable on the total income as computed under this Act without applying the provisions of section 115JA.
6. In case the amount of tax credit allowed can be reduced or increased as per orders u/s 143(1), 147, 154, 155, 245D(4), 250, 254, 260, 262, 263 or 264.

SPECIAL PROVISIONS RELATING TO TAX ON DISTRIBUTED PROFITS [Section 115-O]

1. Tax on distributed profits of companies

In addition to income tax chargeable on the total income of a domestic company and such company has declared, distributed or paid some amount by way of dividends [whether interim or final] on or after 1.6.1997 whether out of current or accumulated profits, it shall have to pay additional income tax at the rate of 10% on amount of dividend so declared, distributed or paid. Such tax shall be known as tax on distributed profits.

2. Responsibility to deposit tax

The principal officer of such domestic shall be liable to deposit tax on distributed profits to the credit of Central Government within 14 days of the date of declaration of dividend.

3. Final payment

The amount of tax on distributed profits deposited as per above shall be considered as final and no further credit shall be claimed by such domestic company or any other person.

4. No deduction

The company or any shareholder of such company shall not have any right to claim any deduction for the amount of tax paid under this section.

With effect from assessment year 1998-99 following changes have been made in section 115 :

1. U/s 115A tax rates on royalty received for technical services rendered, are
   (*a*) if agreement was entered on or before 31.5.1997—30%
   (*b*) if agreement was entered after 31.5.1997—20%
2. Due to exemption of dividend from Indian companies u/s 10(33), the words "income from dividend" as given in section 115AC, 115AD and 115C have been replaced by income from "dividends other than dividend referred to in section 115-O".

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Illustration 1. B.B. Ltd., an Indian tea Company having gardens in India and Sri Lanka declares the following particulars of its income for the relevant previous year :

(*i*)	Profits from the cultivation, manufacture and sale of Tea grown in Indian gardens	5,00,000
(*ii*)	Profits from the cultivation, manufacture and sale of Tea grown in Sri Lanka gardens	3,00,000
(*iii*)	Dividends (Gross) from Agricultural Services Ltd. an Indian Company—the entire income of company is agricultural income	20,000
(*iv*)	Dividends (Gross) from a company incorporated in U.S.A. ($ = Rs. 30).	$ 800

Solution

Computation of Total Income of B.B. & Co.

Business Income:	Rs.
Profits from the cultivation, manufacture and sale of Tea grown in India—40% of total income to be considered as Business Income (40% of Rs. 5,00,000)	2,00,000
Other Sources	
Profit from the cultivation, manufacture and sale of Tea grown in Shri Lanka—agricultural income from outside India is not exempted	3,00,000
Dividends (Gross) from Agricultural Services Ltd.	20,000
Dividends (Gross) from a company registered in U.S.A $ 800 = Rs. 800 × 30	24,000
Gross Total Income	5,44,000
Deduction:	
Under Section 80M—disallowed from assessment year 1996-97	Nil
Total Income	5,44,000

Notes: (*i*) Dividends received from a company are chargeable to tax even if they are from agricultural income.

(*ii*) No deduction u/s 80L is admissible to the company assessee.

(*iii*) It is presumed that B.B. Ltd. has distributed dividend for an amount which is more than dividend received from India Company.

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Illustration 2. From the following particulars, compute the total income of Z

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Ltd. an Indian Company.

		Rs.
(*i*)	Interest on securities	2,000
(*ii*)	Business Income	3,00,000
(*iii*)	Dividends	
	(*a*) From an Indian Paper Mills Ltd.	50,000
	(*b*) From another Indian Company B.	20,000

Compute Total Income of Z Ltd. It started manufacturing in 1994-95. It has distributed dividend of Rs. 50,000 only.

Solution

Computation of Total Income of Z Ltd.

	Rs.	Rs.
Profits		3,00,000
Income from Other Sources:		
Dividend from an Indian Company	50,000	
Dividend from Indian Company B	20,000	
Interest on Securities	2,000	
		72,000
Gross Total Income		3,72,000
Deductions:		
U/s 80IA 30% of Profit of 3,00,000		90,000
Total Income		2,82,000

Illustration 3. India Sugar Co. Ltd. is registered as a private company in India. The company manufactures and sells sugar. The Profit and loss A/c of the company for the year ending 31st March 1997 disclosed a profit of Rs. 5,00,000 only. This was arrived at after debiting following expenses:

		Rs.
(*i*)	Expenses incurred on the cultivation of 5,000 quintals of cane—the average market price is Rs. 10 per quintal	50,000
(*ii*)	Expenses incurred on the salaries and wages of staff involved in the installation of new machinery	2,000
(*iii*)	Pension paid to Mr. James, a retired employee living in Kenya with no income-tax deducted at source	3,000
(*iv*)	Depreciation debited	50,000

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(*v*) Debited to Profit and Loss A/c for legal expenses incurred on Income-tax appeal 25,000

(*vi*) Bad debts, previously written-off and allowed as deduction, recovered in the year but not shown as receipt in Profit and Loss A/c 30,000

(*vii*) Allowable depreciation for the year amounting to Rs. 3,65,000 and it includes depreciation on new machinery acquired and installed in the month of July, 1996 for Rs. 1,50,000

Compute total income of company for the assessment year 1997-98.

Solution

Computation of Total Income of India Sugar Co. Ltd.

Business Income	Rs.	Rs.
Profit as per Profit and Loss A/c		5,00,000
Add: Expenses not admissible		
(*i*) Cultivation Expenses of Sugar Cane	25,000	
(*ii*) Salaries paid to staff on installation of new machinery	2,000	
(*iii*) Pension paid to Mr. James	3,000	
(*iv*) Depreciation debited	50,000	
(*v*) Bad debts recovered during the previous year but not shown as receipt	30,000	
		1,10,000
		6,10,000
Less: Expenses Allowed		
1. Cost of Cane (5,000 quintal) produced in the Company's farm @ average market price, *i.e.*, @ Rs. 10 per quintal	50,000	
2. Depreciation	3,65,000	
		4,15,000
Business Profits		1,95,000

Notes: 1. Salaries paid to staff for installation of new machinery is capital expenditure, hence is disallowed.

2. Pension paid to Mr. James cannot be allowed because no tax has been deducted at source in India.

3. Depreciation has been added back because actual amount is allowed later on.

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4. Bad debts recovered during the previous year are the income of the year in which they are recovered, if they were previously allowed as deduction.

5. No deduction of investment deposit account is allowed with effect from assessment year 1991-92.

Illustration 4. Given below is the Profit and Loss Account of Bharat Mills Ltd. for the year ended 31st March, 1997:

	Rs.		Rs.
Cotton	1,14,17,950	Yarn Account	1,08,11,956
Stores	18,35,648	Cloth Account	96,24,312
Mills Salaries & Wages	38,31,984	Waste Account	1,21,108
General Expenses	29,008	Transfer Fees	8,216
Donations	10,000	Rent of Bungalows	
Rates and Insurance	40,376	and Chawls	57,902
Brokerage	7,224	Dividends (Net)	
Office Expenses	2,40,694	from Punjab	
Director's Fees	9,000	National	
Auditor's Fees	5,000	Fertilizers Ltd.	32,000
Interest	2,11,850		
Repairs to Building and			
Machinery	1,24,556		
Law Charges	5,730		
Workmen's Welfare			
Expenditure	55,184		
Contribution to Staff			
Provident Fund	75,500		
Managing Agent's			
Commission	2,01,090		
Net Profit (subject to			
depreciation)	25,54,700		
Total	2,06,55,494	Total	2,06,55,494

From the foregoing ascertain the company's taxable income from business and also the total income for the income-tax assessment year 1997-98 taking the following into account:

(*a*) Rs. 1,824 of brokerage was paid for cotton and stores purchases, and the balance was in respect of loans for the company's business.

(*b*) Rates Rs. 3,600 insurance Rs. 2,500 and repairs to building Rs. 5,744 were in respect of bungalows and chawls let to employees.

(*c*) Legal charges amounting to Rs. 1,900 were incurred in connection with the purchase of additional land and buildings.

(*d*) The Staff Provident Fund is a recoginzed one.

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(*e*) The amount of depreciation allowance for assets used for the company's business is worked out at Rs. 5,51,710.

(*f*) Company has distributed dividend of Rs. 10 lakhs to its shareholders.

Solution

Profits and gains of Business or Profession	Rs.	Rs.
Net Profit before charging Depreciation		25,54,700
Less: Incomes to be treated under separate Heads		
Rent of Bungalows & Chawls	57,902	
Dividends	32,000	
		89,902
		24,64,798
Add: Inadmissible deductions		
Donations	10,000	
Rates, insurance & repairs related to building let	11,844	
Legal charges of capital nature	1,900	
		23,744
		24,88,542
Less: Allowable depreciation:		5,51,710
Business Income		19,36,832
Income from House Property:		
Rent received	57,902	
Less: Rates	3,600	
Annual Value	54,302	
Deductions Rs.		
1/5th of A.V. for repairs 10,860		
Insurance 2,500		
	13,360	
House Property Income		40,942

COMPUTATION OF TOTAL INCOME

House Property Income	40,942
Business Income	19,36,832
Other Sources	
Dividends (Net) 32,000, Gross (32,000 × 100/80)	40,000
G.T.I	20,17,774

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Deductions:

u/s 80G: Deduction regarding Donations

Q.A=Rs. 10,000 50% of Q.A.	5,000
Total Income	20,12,774

Rounded off to Rs. 20,12,770

Illustration 5. M/S M. Textiles Ltd furnishes the following particulars in respect of its business for the period 1-4-96 to 31-3-97 and you are requested to compute its total income:-

I. *P & L Appropriation Account:*

	Rs.
(*i*) By Net Profit carried down from P & L A/c	2,00,000
(*ii*) By cash assistance received from Govt. against exports	3,00,000
(*iii*) By duty drawback against exports	3,00,000

II. *Land Account (Acquired in 1989-90) [C.I.I. 172]*

	Rs.		Rs
To balance B/F	7,00,000	By Sale [C.I.I. 305]	13,00,000
To excess carried to capital A/c	6,00,000		
	13,00,000		13,00,000

III. *Plant & Machinery Account*

To balance B/F	12,00,000	By Depreciation	4,00,000
To excess carried to capital A/c	12,00,000	By sale	20,00,000
	24,00,000		24,00,000

IV. *Technical Know How Account*

To Purchase of Technical Know how from Govt. Laboratory (Govt. of India)	300,000	By Balance C/F	3,00,000
	3,00,000		3,00,000

Further details are as under :—

(*a*) Salaries & wages account include

(*i*) a sum of Rs. 1 Lakh paid towards hospitalisation and surgery charges of the managing director.

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(*ii*) Contribution paid towards the recognized provident fund paid on 1-5-96 by cheque which was realised on 17.5.96..... Rs. 100,000.

(*b*) Export Turnover Rs. 120 Lacs, Total turnover Rs. 300 Lacs

(*c*) Business Loss, B/F from the previous year 1995-96 Rs. 8 Lakhs.

(Adapted C.A Final. May, 1991)

Solution

Computation of Business Income		Rs.
Net Profit as per P& L A/c		2,00,000
Add:		
(*i*)	Cash assistance received from Govt. against exports	3,00,000
(*ii*)	Duty draw back against exports	3,00,000
(*iii*)	Depreciation (as debited in P & L A/c)	4,00,000
(*iv*)	Personal medical expenses of managing director (It can be allowed as managing director is employee of the company and if treatment is taken from a Govt. Hospital or approved hospital it is exempted perquisite in the hands of employee. On the basis of this arrangement the expenditure incurred under the head salaries to employees can be debited to P & L A/c. But u/s 40 A(2) the Assessing Officer can raise the objection of its being unreasonable or excessive or not in the interest of business. Hence disallowed u/s 40 A(2)	1,00,000
(*v*)	Contribution to R.P.F.—disallowed u/s 43B as payment was made by cheque and cheque was not realised within 15 days, hence disallowed u/s 43B	1,00,000
	Total	14,00,000
Less:		
(*i*)	Expenditure on Technical know how made to a laboratory owned by Govt. Allowed u/s 35AB 1/3 rd of actual expenditure 100,000	
(*ii*)	Depreciation-not allowed as asset was sold during the year Nil	1,00,000
Income from Business		13,00,000

Computation of Total Income

Profits & Gains	Rs.	Rs.
(*a*) Business Income	13,00,000	
(*b*) Set off B/F Business loss of 95-96	8,00,000	
		5,00,000

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Capital Gain

Short Term capital Gain u/s 50		
Money realised on sale of P & M	20,00,000	
Less: W.D.V. on 1-4-96	12,00,000	
S.T.C. Gain	8,00,000	
Long Term capital Gain on Land		
Sale Price of Land Rs. 13,00,000		
Cost Price of Land Rs. 12,41,279		
[7,00,000 × 305/172]		
L.T.C. Gain	58,721	
		8,58,721
Gross Total Income		13,58,721
Deduction u/s 80HHC: Proportionate profits is allowed as deduction [500,000 × 120 lacs/300 lacs)		200,000
Total Income		11,58,721

Rounded off to Rs. 11,58,720

Q. No. 1

Ashwani Company Pvt. Ltd, furnish the following information:

	Rs.
Interest on securities (computed)	10,000
Income from House property (computed)	20,000
(*a*) Textile manufacturing :	
Profit as per P. & L. A/c before depreciation	2,00,000
Depreciation	95,000
(*b*) Hosiery manufacturing :	
Profit as per P. & L. A/c before depreciation	75,000
Depreciation	18,000
Agency business Loss b/f from 1992-93	15,000
Income from other sources	25,000

Compute the total Income for the assessment year 1997-98.

[Company Secretaries Final]

[Hints: Profits and Gains Rs. 1,62,000 other sources Rs. 40,000 Total Incomes Rs. 2,22,000] [P-1]

Q. No. 2

Prakash Traders Limited as a company in which the public are substantially interested. It closes its accounts on 31st March every year. During the current year, it has derived the following incomes;

(*a*) Profit from the manufacturing unit at Lucknow Rs. 3,20,000.

(*b*) Profit from trading activities at Lucknow Rs. 1,00,000.

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(*c*) Dividends from another company which is a domestic company producing cement Rs. 25,000 (gross) No dividend was distributed by M/s Prakash Traders Ltd.

(*d*) Dividends from a foreign company Rs. 15,000.

(*e*) Profit from a newly started and approved hotel Kanpur Rs. 2,10,500. Capital employed being Rs. 15,000,000 and Normal Depreciation Rs. 60,000 has not been charged in the calculation of above profit.

(*f*) The company passed on a certain formula for manufacturing tiles to another company in Uganda and received royalty therefrom Rs. 2,10,000.

(*g*) Brought forward unabsorbed depreciation Rs. 24,000 and unabsorbed Investment Allowance Rs. 15,000 from the assessment year 1989-90.

You are required to calculate total income of the company.

[B.H.U., M.Com.]

[**Hints :** Profits & Gains Rs. 5,31,500; Other Sources Rs. 2,45,000 Deduction u/s 80IA Rs 33,450, 8 ; 80 O Rs. 1,05,000 Total Income Rs. 6,38,050] [P-2]

Q. No. 3

An Indian company carries on business in Motor Transportation. Its Profit & Loss Account for the previous year 1996-97 shows a net profit of Rs. 2,80,250. Find out Gross Total Income on the company after taking into consideration the following particulars.

The Profit % Loss Account was debited with following expenses :

(*i*) Rs. 2,50,000 as depreciation.

(*ii*) Rs. 18,750 as Bad Debt reserve.

(*iii*) Rs. 10,000 spent to obtain a new licence and the company was able to get it.

(*iv*) The engine of a very old bus was replaced by a new one by spending Rs. 60,000.

(*v*) Mr. X, a retiring director, was paid Rs. 60,000 as gratuity in appreciation his services. In the past, the company never paid such a gratuity to any of its retiring directors and even the service conditions did not provide for the payment of such gratuity.

The Profit and Loss Account was found credited with following incomes:

(*i*) Agricultural receipts of Rs. 65,000.

(*ii*) Rs. 7,760 received as not dividend from an Indian Co. producing cement.

(*iii*) Sale proceeds of old tyres etc. Rs. 2,000.

(*iv*) Capital gain on sale of Motor Car Rs. 20,000. (Short Term).

An per the rates applicable in the current year, the amount of depreciation comes to Rs. 1,65,000.

[**Hints :** Business Income Rs. 4,11,240, S.T.C.G. Rs. 20,000 other Sources Rs. 10,000 GTI Rs. 4,41,240] [P-3]

Q. No. 4

Fancy Garments Limited is a domestic company, in which the public are substantially interested. For the year ended 31-3-1997 the profit and Loss Account of the company shows a net profit of Rs. 20 lakhs. On inquiries it has given the following information :

Amounts debited to Profit & Loss Account :

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(*a*) Rs. 18,000 spent by the managing director on his visit to Canada. The visit was for studying the market for exports.

(*b*) Rs. 20,000 representing cost of garments donated to an approved charitable trust.

(*c*) Rs. 23,000 on account of expenditure of maintenance of guest house at factory.

(*d*) Rs. 18,000 paid to an associate member of the Institute of Chartered Accountant of India for attending to income tax appeals for two years before the Income Tax Appellate Tribunal.

(*e*) Rs. 9,500 paid to a money-lender as interest taken to meet the company's income tax liability.

(*f*) Penalty of Rs. 4,000 paid for importing garments manufacturing machinery in contravention of import regulations.

Other informations :

(*g*) The company has set up a gratuity fund. A sum of Rs. 50,000 has been debited for *accrued liability to staff*. The provision has been made in the accounts. The quantum of the liability has been worked out on well recognised actuarial basis.

(*h*) Rs. 25,000 credited in the Profit & Loss Account on account of dividend received from a foreign company. The shares in the foreign company were allotted in consideration of technical know-how under a collaboration agreement approved by the Central Board of Direct Taxes.

(*i*) The company suffered long-term capital loss in earlier years as under :

Assessment Years			
1992-93	1994-95	1995-96	1996-97
Rs. 50,000	Rs. —	Rs. —	Rs. 75,000

Compute the Gross Total Income of the company for the assessment year 1997-98.

[**Hints :** Business Income Rs. 20,31,500 other sources Rs. 25,000 G.T.I. Rs. 20,56,500; Expenses on MD's visit allowed; Provision for gratuity is allowed; No deduction u/s 80G for donation in kind; L.T.C. Loss of A.Y. 1992-93 to be written off and of A.Y. 1996-97 to be C/F] [P-4]

Q. No. 5

The Manufacturing Company Ltd. has given the fallowing particulars for computation of its total income and filing its return before the Assessing office for the Assessments year 1997-98 :-

(*a*) Net profit for the year ending 31-3-1997 was Rs. 5,00,000.

(*b*) Depreciation has been charged in the accounts at rates prescribed by the Income-tax Rules.

(*c*) The following assets were purchased and used in the business from 15-1-1997 and has been debited in the machineries account. Depreciation has been charged on them for 12 months :

	Cost	Rate of depreciation
Calculating machine	5,000	25%
Second-hand typewriter	4,000	25%
Cycle	700	25%

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(*d*) Expenditure on advertisements in India amounted to Rs. 1,30,000 as against Rs. 1,50,000 in the preceding year.

(*e*) The company has 10 motor cars for its factory in Bihar and 8 cars for the head office and branches in India. Total expenditure on motor cars was Rs. 1,50,000 excluding the salary for Rs. 50,000 paid to the drivers and debited to the "Establishment A/c".

(*f*) Demand notices for sales tax and excise duty totalling Rs. 70,000 were received on 28-3-97 payable on or before 28-4-97. The liability has been provided for in the accounts for the year ending 31-3-97 and was paid on 10-1-1998.

(*g*) For the first time the company secured an export order in response to an advertisement inserted in a newspaper in the U.K. during the year at a cost of Rs. 40,000 and the goods were exported in April, 1997.

(*h*) The net profit for the year has been determined after debiting capital expenditure of Rs. 50,000 on scientific research under Section 35 (2) (ia) of the Income-tax Act.

(*i*) Donation of Rs. 1,00,000 to the Prime Minister's Drought Relief Fund has already been debited to the Profit & Loss A/c for this year.

(*j*) There is an unabsored investment allowance of Rs. 3,33,333 for the previous year 1989-90 for which necessary reserve has been created this year.

You are required to show the computation of Total Income and also the carry forward of unabsorbed allowances, if any, with appropriate notes.

[I.C.W.A. Final]

[**Hints** ; Profits & Gains being GTI (after adjustment of B/F investment Allowance) Rs. 3,37,879; Deduction u/s 80G Rs. 50,000 Total income Rs. 2,87,879; 1/2 depreciation to be added back as new assets were used for less than 180 days] [P-5]

Q. No. 6

XYZ, a domestic company (in which public are substantially interested) in manufacturing textiles. For the year ending 31-3-97, the P. & L. A/c showed a net profit of Rs.. 10,00,000 on a turnover of Rs. one crore. This included following debits to P. & L. A/c :—

(*i*) Dividends amounting to Rs. 20,000 paid to the share holders for the accounting years 1995-96.

(*ii*) Interest amounting to Rs. 10,000 paid on the loan taken for the payment of the company's income-tax liability.

(*iii*) Interest amounting to Rs. 15,000 paid on the loan taken to make donation to an approved charity.

(*iv*) (*a*) Rs. 20,000 spent by the managing director on his visit to :

(*i*) Canada to buy machinery and finalise a collaboration agreement for a new independent undertaking proposed to be set up (cement factory) Rs. 10,000.

(*ii*) USA to study export market for textiles—Rs. 10,000.

(*b*) Managing Director's wife accompanied her husband—Rs. 10,000 was contributed by the company towards her foreign trip expenses and the Canadian collaborator paid Rs. 15,000 to her towards expenses.

(*v*) Company incurred Rs. 25,000 as entertainment expenditure.

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(*vi*) Company incurred expenditure of Rs. 1,00,000 as follows :
  (*a*) advertisement in newspaper Rs. 50,000.
  (*b*) advertisements in Souvenir of a political party Rs. 25,000.
  (*c*) guest house at factory Rs. 35,000.

(*vii*) Rs. 20,000 paid to legal advisers in respect of proceedings before income-tax authorities.

(*viii*) Penalty of Rs. 24,000 for importing yarn in contravention of important regulations.

Compute the taxable income of the company.

[Company Secretaries, Final]

[**Hints :** Dividend, interest on loan for income tax or charity, foreign expenses of M.D., M.D.'s wife, advertisement in souvenir of political partly, guest house expenses, penalty—fully disallowed. Entertainment Exp. disallowed Rs. 7,500 Company's business income Rs. 11,56,500] [P—6]

QUESTIONS

1. What are the salient features of assessment of Joint stock companies ?
2. Explain in brief the various deductions u/s 80 which can be claimed by a company ?
3. Explain the provisions of law regarding companies in which public are substantially interested.
4. Write notes on (*i*) company (*ii*) Indian company (*iii*) Residence of a company (*iv*) conditions for set off and carry forward of losses on amalgamation of companies.

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5 Assessment of Co-operative Societies

Cooperative society and its types—Computation of total income—Deductions u/s 80—Illustrations and Questions.

In a country like India, which had adopted socialistic pattern of society, the co-operative societies have to play an important role and to encourage them, they have to be put in privileged position. One of the privileges which the co-operative societies enjoy is in respect of income-tax payable by them.

Co-operative Society—Definition. "Co-operative society" means a society registered under the Co-operative Societies Act, 1912 (II of 1912) or under any other law for the time being in force in any State for the registration of co-operative societies [Section 2(19)].

Urban Consumer's Co-operative Society. Under section 80P(2) (explanation), such a society has been defined as "a society for the benefit of the consumers within the limits of a municipal corporation, municipality, municipal committee, notified area committee, town, area or cantonment".

Computation of Total Income. The total income of a Co-operative Society is to be computed in accordance with the different provisions of the Income-tax, Act, 1961. The income is to be computed headwise.

Deductions from Total Income

Section 80P of the Act provides certain deductions which are to be allowed out of Gross Total Income of the society. Under the provisions of this section certain incomes which form part of Gross Total Income are to be deducted because Income-tax is not payable by the Co-operative Society in respect of these incomes:

Society 80P(1) provides that out of Gross Total Income of a co-operative society the incomes described in sub-clause (2) of this section shall be deducted.

Section 80P(2) provides that following incomes shall be deducted out of Gross Total Income—

(*a*) Income of a co-operative society engaged in following activities, *shall be deducted:*

(*i*) carrying on the business of banking or providing credit facilities to its members; or

(*ii*) a cottage industry; or

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(*iii*) the marketing of the agricultural produce of its members; or

(*iv*) the purchase of agricultural implements, seeds, livestock, or other articles intended for agriculture for the purpose of supplying them to its members; or

(*v*) the processing (without the aid of power) of the agricultural produce of its members; or

(*vi*) the collective disposal of the labour to its members; or

(*vii*) fishing or allied activities, *i.e.*, the catching, curing, processing, preserving, storing or marketing of fish or the purchase of materials and equipment in connection therewith for the purpose of supplying to its members.

For sub-clauses (*vi*) & (*vii*), 80P (2) further provides that the rules and by-laws of the society must restrict the voting right to the following classes of its members;

(*i*) the individuals who contribute their labour, or as the case may be, carry on the fishing or allied activities;

(*ii*) the co-operative credit societies which provide financial assistance to the society;

(*iii*) the State Government.

(*b*) The whole of amount of profits and gains from the business of supplying milk, oil seeds, fruits or vegetables by the members of primary co-operative society to a federal milk co-operative society, or the Government or local authorities or a Government Company.

(*c*) A deduction of Rupees 40,000 shall be allowed to all other Co-operative Societies which are engaged in any business which is not specified in clause (*a*) and (*b*) above.

(*d*) Whole of the income from dividend or interest or investments of one co-operative society with any other co-operative society will be allowed as deduction.

(*e*) Whole of the income of a co-operative society derived from the letting of godowns or by warehouses for storage, processing or facilitating the marketing of commodities shall be allowed as deduction.

(*f*) The whole amount of interest on securities or income from house property of a co-operative society provided;

(*i*) the gross total income of the society does not exceed Rs. 20,000.

(*ii*) it is not a housing co-operative society, or an urban consumer society or a society carrying on transport business.

(*iii*) it is not a society engaged in the performance of any manufacturing operations with the aid of power.

Concession u/s 27(iii) : Co-operative Housing Society

If a house is allotted or leased out by a Co-operative Society to its member but the ownership remains with co-operative society the income from such house property shall form a part of the total income of the individual.

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Other Deductions

Every co-operative society is entitled to claim deduction u/s 80IA (with effect from 1.4.91). The benefit of deduction u/s 80IA shall be available for new industrial undertaking or ship or hotel for a period of 12 years.

Illustration 1. The Ludhiana Co-operative Marketing Society is a society registered under the Co-operative Societies Act, 1912 and is engaged in the business of purchase of agricultural implements and seeds for the purpose of supplying them to its members. From this business it earned an income of Rupees 50,000.

In May 1980 it opened a consumer's store for selling groceries and this venture netted a profit of Rs. 55,000 during the year 1996-97. Compute the total income of society and tax payable by it for the assessment year 1997-98.

Solution

1. Whole of income from the business of purchase of agricultural implements and seeds to its members is allowed as deduction under section 80 P (2) sub-clause (*a*) (*iv*).

2. Out of the profits of Rs. 55,000 from the consumer's store Rupees 40,000 are exempted from tax under section 80 P (2) sub-clause (*c*).

		Rs.
Income from Purchase of Agricultural Implements		50,000
Income from Business of Consumers' Store		55,000
Gross Total Income		1,05,000
Deductions:		
Whole of income from agricultural implements	50,000	
Profits from Consumers' Store [80 P(2) (c)]	40,000	
		90,000
Total Income		15,000

Thus the total taxable income of society is only Rs. 15,000.

Computation of Tax

Income-tax on Rs. 15,000 =	First 10,000 @ 10%	1,000
	Next 5,000 @ 20%	1,000
	Total Tax	2,000

Illustration 2. The Government College Co-operative society Ltd. has the following incomes during the year:

	Rs.
(*a*) Income from College Canteen & Mess	20,000
(*b*) Income from College Book Shop	8,000
(*c*) Interest on Securities (Gross)	8,000
(*d*) Income from House Property (computed)	5,000
(*e*) Dividend on shares of another Co-operative Society	13,000

Compute the total income of society.

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Solution

		Rs.
1. Income from house property (computed)		5,000
2. *Profit from Business:*		
(*i*) from Canteen Mess	20,000	
(*ii*) from Book Shop	8,000	
		28,000
3. *Income from Other Sources:*		
Dividend from Co-operative Society	13,000	
Int. on Securities (Gross)	8,000	
		21,000
Gross Total Income		54,000
Deduction u/s 80 P		
u/s 80 P (2) (c) Business Income	28,000	
u/s 80 P (2) (d) Dividend from another Co-operative Society	13,000	
		41,000
Total Income		13,000

Note: As the gross total income of the society exceeds Rs. 20,000 so the deduction of interest on securities and house property u/s 80 P (2) (f) shall not be allowed.

Illustration 3. The Chandigarh Urban Consumer's Co-operative Society Ltd., derived the following incomes in the year ending 31st March.

1. Income from Business	21,000
2. Dividend (Net) on shares in Oswal Woollen Mills Ltd.	4,800
3. *Interest on fixed deposits with:*	
(*i*) Central Consumer's Co-operative Society, Chandigarh	2,000
(*ii*) Indian Bank	3,000
4. Rent from 1/3 of building let out to an outsider; 2/3 being used by the society for its own business	2,000

Expenses for the building:

	Rs.
(*i*) Municipal Taxes	600
(*ii*) Ground Rent	150
(*iii*) Insurance	300

Compute the total income of the Society.

Solution

Computation of the total income of the Co-operative Society

	Rs.	Rs.	Rs.
1. *Income from House Property*			
Rental Value—1/3 of building	2,000		
Less: Taxes 1/3 of 600	200		
Annual Value		1,800	

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Deductions:			
1/5th of A.V. for repairs	360		
1/3rd of Ground Rent	50		
1/3rd of Insurance Premium	100		
		510	
2. *Income from Business*			1,290
		21,000	
Less: Expenses on house being used for the business of society			
2/3rd of Ground rent	100		
2/3rd of Insurance Premium	200		
		300	
			20,700
3. *Income from other sources*			
(*i*) Dividend (Net) Rs. 4,800 Grossed up (4,800 × 100/80)	6,000		
(*ii*) Interest on fixed deposits:			
(*a*) with Co-operative Society	2,000		
(*b*) with Indian Bank	3,000		
			11,000
Gross Total Income			32,990
Deductions u/s 80 P			
Business Profits u/s 80 P (2) (*c*)	20,700		
Interest on Deposit with Co-operative Society u/s 80 P (2) (*d*)	2,000		
			22,700
Total Income			10,290

QUESTIONS

1. How the assessment of co-operative society is made ? What are the tax incentives available to a co-operative type of Assessee ?
2. Describe in details the provisions of Income-tax Act regarding the assessment of co-operative societies.

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6 ASSESSMENT IN SPECIAL CASES

Computation of tax liability on income on which no tax is payable—Tax on accumulated balance of RPF—Tax on Long Term Capital Gains—Tax on Dividend, Royalty or fee received by Foreign companies—Tax on capital gain on Bonds purchased in foreign currency—Tax on Gain of life insurance business—Tax on winning from lotteries, crossword puzzles, races etc.—Tax on non-resident sports association—Tax on non-residents—Amendments made by the Finance Act 1992—Questions.

Tax liability on income on which no tax is payable [Section 110]

In case any income on which no tax is payable under this Act, is included in the total income of an assessee, out of the income-tax on total income, he shall be entitled to deduction of tax calculated at average rate, on such income. These incomes are:

(*a*) Share of income from a partnership firm which is assessed as A.O.P. under Income-tax Act 1961; or

(*b*) Share of income from an association of persons provided the total income of firm assessed as A.O.P. or A.O.P. exceeds the exempted limit. *(The detailed treatment of this point is given in chapter 2 of part III of this book).*

Tax on accumulated balance of recognised provident fund [Section 111]

In case the accumulated balance of R.P.F. of an employee is included in his total income because the provision of Rule 8 of Part A of the fourth schedule are not applicable, the Assessing Officer shall calculate the total of various sums of tax in accordance with the provisions of sub-rule (1) of rule (9) of 4th schedule. This section provides for adding the year-wise break up of balance in respective year's income and then calculating the tax payable on such addition. Under rule 10 of 4th schedule the person responsible for making the payment of accumulated balance of RPF is required to deduct tax at source treating such balance as if it is income taxable under the head *'Salaries'*.

Tax on Long Term Capital Gains [Section 112]

A. With effect from assessment year 1993-94, in case total income of an assessee includes long-term capital gain, the tax payable shall be—

(a) In case of individual or HUF being a Resident

(*i*) Tax @ 20% of long term capital gain; and

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(*ii*) Tax at prescribed rates on total income as reduced by long term capital gains;

(*iii*) In case after deducting long-term capital gain from total income, balance is less than exempted limit, the long term capital gain shall be reduced by an amount by which the balance income falls short of exempted limit. Rest of long term capital gain shall be taxable @ 20%.

(*b*) *In case of firm, an association of persons or body of individuals*

(*i*) Tax @ 20% of long term capital gain; and

(*ii*) Tax at prescribed rates on total income as reduced by long term capital gain.

(*c*) *In case of domestic company –30%.*

(*d*) *In case of a non resident (other than Companies) or a foreign company.*

(*i*) Tax @ 20% on long term capital gain ; and

(*ii*) Tax at prescribed rates on total income as reduced by long term capital gain.

(*e*) *In any other case of a resident*

(*i*) Tax @ 20% of long term capital gain; and

(*ii*) Tax at prescribed rates on total income as reduced by long term capital gain [Section 112(1)].

B. In case gross total income consists of long term capital gain and other incomes, the long term capital gain shall be deducted out of gross total income and deductions u/s 80 shall be allowed only out of balance G.T.I. [Section 112(2)].

C. In case total income of an assessee includes long term capital gain, total income shall be reduced by such long term capital gain and rebate u/s 88 shall be allowed only out of tax on such balance total income [Section 112(3)].

Tax on dividends, royalty and technical service fee in case of foreign companies [Section 115A]

(*a*) In case of dividends included in total income, tax is to be charged @ 20% of such dividend income.

(*b*) In case of interest received from Government or an Indian concern on moneys borrowed or debts incurred by Government or the Indian concern in foreign currency, tax is to be charged at the rate of 20% of such interest included in total income.

(*c*) In case of income by way of interest on units of Mutual Funds (as specified u/s 10(23D)] and such units are purchased with foreign currency, tax is to the charged @ 20% of such interest included in total income.

(*d*) In case any royalty or fee is received for technical services provided to Government or an Indian concern under an agreement entered after 31.3.76 the tax is to be charged @ 30% of such royalty or fee included in total income. The agreement with Indian concern is to be approved by the Central Government. In case of royalty which is for transfering all rights in respect of copyright in book to Indian concern or in respect of any computer software to a person resident in India however, the approval of Central Government is not necessary.

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(*e*) Out of the total income of such foreign companies the incomes as given in (*a*) to (*d*) above shall be deducted and balance income, if any, shall be taxable at scheduled rates.

Amendment in Section 115A relating to tax on dividends etc.

Where the approval of the Central Govt. is required the new provision is that if the agreement relates to a matter included in the industrual policy for the time being in force, the agreement should also be in accordance with this policy.

Tax on capital gain on sale of Bonds purchased in Foreign currency [Section 115AB]

1. Where the total income of an assessee being an overseas financial organisation (offshore fund) includes income received in respect of units purchased in foreign currency—the income tax shall be calculated at the rate of 10% of such income included in total income.
2. Where the total income of an assessee being an offshore fund includes long term capital gain arising from the transfer of units purchased in foreign currency, the income-tax shall be calculated at the rate of 10% of such long-term capital gain included in total income.
3. Out of total income of such offshore fund, the incomes given at (1) and (2) above shall be deducted and balance total income shall be taxable at scheduled rates.
4. While calculating the incomes given at (1) and (2) above
   (*a*) If the total income of such offshore fund consists only of these incomes, no deduction u/s 28 to 44C, 48(2) or 57(i) or 57(iii) shall be allowed. The fund shall not be entitled to claim any deduction u/s 80;
   (*b*) If the total income of offshore fund consists of these incomes and other incomes as well, the gross total income shall be reduced by such incomes; and out of balance G.T.I. deductions u/s 80 shall be allowed.

Insertion of New section 115AC regarding tax on Capital Gain from sale of Bonds or shares purchased in foreign currency

In case total income of a non-resident includes—

(*a*) any income by way of interest or dividend on bonds or shares of an Indian company issued in foreign currency and purchased in foreign currency (under a scheme notified in Official Gazette) *or on bonds or shares of a public sector company, sold by Government (from 1.10.96)*—tax will be levied on such income @ 10%.

(*b*) any income by way of long term capital gain arising from the transfer of bonds or shares as referred above,—tax will be levied @ 10% of such long term capital gain.

(*c*) the balance of total income shall be assessed to tax at scheduled rates.

(*d*) In case of interest or long term capital gain on such bonds or shares, no deduction u/s 28 to 44C or clause (*i*) and (*iii*) of section 57 or u/s 80 shall be allowed. In case assessee has any other income, he shall be eligible for deductions u/s 80 only out of balance gross total income.

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Tax on income of Foreign Institutional Investors from securities or Capital gain on transfer of securities [Section 115AD]

Tax will be levied on a Foreign Institutional Investor at following rates :

(*i*) If total income includes income from securities [Except units mentioned u/s 115 AB] — such income will be assessed at the rate of 20% on such interest;

(*ii*) If total income includes short-term capital gain on such securities tax will be levied at the rate of 30% on such short term capital gain;

(*iii*) If total income includes long term capital gain on such securities, tax will be levied @ 10% on such long term capital gain; and

(*iv*) On balance total income tax will be levied at prescribed rates.

The Foreign Institutional Investor shall not be allowed any deduction u/s 28 to 44 AC or u/s 57 (*i*) or (*ii*) of the Act out of income from interest on securities. For deductions u/s 80 gross total income shall be reduced by the incomes referred above.

Tax on Gain from life insurance business [Section 115B]

In case the total income of an assessee includes any profits and gains from life insurance business, the income tax @ 12.5% of such profits and gains, shall be payable. The total income of the assessee is to be reduced by the profits & gains of life insurance business and balance is to be taxed at scheduled rates.

Tax on winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or gambling or betting [Section 115BB]

In case any of these incomes is included in total income of an assessee, tax will be calculated as under:—

(*i*) Income from any of these sources—40%.

(*ii*) Balance total income at scheduled rates.

Tax on Non-resident sportsmen or sports association [Section 115BBA]

In case of an assessee who is not citizen of India and who is not resident in India, any of the following incomes is included in total income—

Any income received or receivable by such person by way of

(*i*) participation in India in any game (except those covered u/s 115 BB) or sport; or

(*ii*) advertisement; or

(*iii*) contribution of articles relating to any game or sport in India in newspapers, magazines or journals; or

(*iv*) any amount received or receivable by a non-resident sports association on institution as guarantee amount in relation to any game or sport in India—tax will be levied at the rate of 10% on such incomes and balance of total income shall be assessed at scheduled rates. No deduction of any expenditure is allowed out of these incomes.

In case such an assessee has only such income which is covered under point (*i*) to (*iv*), he is not required to file the return of income u/s 139(1) if tax has been deducted at source. [115 BBA(2)]

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Tax on Non-Residents [Section 115C to 115-I]

1. Computation of total income of a non-resident [Section 115D]

(*i*) In case of a non-resident Indian assessee, no expenditure or allowance shall be allowed under any of the provisions of this Act.

(*ii*) In case the gross total income consists only of investment income or income by way of long-term capital gain or both, no deduction u/s 80 shall be allowed.

(*iii*) In case gross total income consists of incomes as given above in (*i*) and other incomes, the G.T.I. shall be reduced by such incomes which will be treated as per (*ii*) above and out of balance GTI deductions u/s 80 shall be allowed.

2. Tax on investment income and long-term capital gains [Section 115E]

(*i*) In case total income consists of only investment income and long-term capital gain, it will be taxable at the rate of 20%.

(*ii*) In case total income consists of investment incomes, long-term capital gain and other incomes, tax will be levied at the rate of 20% of investment income and long-term capital gain and balance of total income shall be assessed at scheduled rates.

3. No tax on capital gain on transfer of foreign exchange assets [Section 115F]

In case total income of Non-resident Indian includes long-term capital gain arising from transfer of a foreign exchange asset and such person has invested some amount in specified asset, or any savings certificates as referred in section 10(4B) within 6 months from transfer, proportionate capital gain to be calculated as under shall be fully exempted—

(*a*) in case whole of net consideration is invested, whole of capital gain shall be exempted; and

(*b*) in case a part of the net consideration is invested, the exemption shall be—

Exempted C. Gain = LTCG × Amount invested/Net consideration

Net consideration means the full value of consideration reduced by any expenditure incurred on transfer.

'*Specified asset*' as defined u/s 115C includes:

(*i*) shares of Indian company;
(*ii*) debentures issued by an Indian public limited company;
(*iii*) deposits with Indian public limited company;
(*iv*) Securities issued by Central Govt. and so notified;
(*v*) any other asset so notified by the Central Government.

In case NRI claims exemption under this section by investing in specified assets or savings certificates, such new asset cannot be transferred or converted into money within a period of *three years*. The exemption claimed earlier shall be deemed as income under the head 'capital gain' as L.T. capital gain of the previous year in which new asset is transferred or converted into money.

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4. Return of income not to be filed [Section 115G]

The non-resident Indian who has income from investments or long-term capital gain or both is not required to file a return of income u/s 139(1) if tax at source (if required) has been deducted.

5. Continuance of benefit even after becoming Resident [Section 115H]

The non-resident Indians have been given an option of being governed by these provisions even after becoming resident if they give a declaration to the Assessing Officer along with return u/s 139(1). He will be governed by these provisions in case of income from investments till the investments are converted into money or are transferred.

6. Option to assessee [Section 115-I]

In case the non-resident Indian gives a declaration in writing to the Assessing Officer alongwith return u/s 139(1) that the provisions of section 115D to 115H may not be applied to him, he will be governed by other provisions of this Act.

PROVISIONS OF MINIMUM ALTERNATIVE TAX ON COMPANIES (MAT) [Section 115 JA]

1. These provisions are applicable on all those Indian companies whose total income as computed under this Act in respect of any previous year relevant to the assessment year commencing on or after 1.4.1997, is less than 30% of book profits.
2. For the purposes of levying tax on such companies total income as computed under Income-tax Act shall be disregarded and **30% of Book profit** shall be deemed as total income for such previous year.
3. Every such company shall prepare its profits and loss account in accordance with the provisions of part II and III of Schedule VI of the Companies Act 1956.
4. While preparing profit and loss account **depreciation will have to be the same as has been charged for preparing the accounts to be presented at the time of annual general meeting of the company.** In case the company has its accounting year which is different than financial year the amount of depreciation (as mentioned above) shall have to be adjusted.
5. The term Book profit means the net profit as per profit and loss account which is to be increased by the following if these are debited or are not credited to P & L A/c :
   (*a*) any amount of income-tax paid or payable and any provision for such tax,
   (*b*) any amount carried to any reserve by whatever name called,
   (*c*) any amount set aside to meet any liability other than ascertained liabilities,
   (*d*) any amount set aside as provision for losses of subsidiary companies,
   (*e*) any amount or amounts of dividend paid or proposed,
   (*f*) any amount of expenditure relating to such incomes which do not form part of total income u/s 10 to 13.

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Amount so arrived at shall be reduced by the following :

(*i*) any amount withdrawn from reserves other than reserve specified u/s 80 HHD, or from provisions, if any such amount is credited to the P & L Account. Any amount withdrawn from a reserve created or provision made on or after 1.4.1997, the amount of said withdrawal shall not be deducted if such amount has not increased the book profits of such year.

(*ii*) any income which is not to be included in total income as given u/s 10 to 13 but has been credited.

(*iii*) any amount of loss brought forward or unabsorbed depreciation which ever is less, [B/F loss shall not include unabsorbed depreciation].

(*iv*) any amount of profits derived by an undertaking from the business of generation and distribution of electricity.

(*v*) any amount of profits derived by an undertaking set up in industrially backward districts as notified u/s 80IA during the period it is eligible for deduction u/s 80IA.

(*vi*) any amount of profits derived by an undertaking set up in infra structural sector as notified u/s 80IA during the period it is eligible for deduction u/s 80IA.

(*vii*) any amount of profits of a sick industrial company for the period from the assessment year in which the unit became industrially sick till the assessment year during which the entire net worth of the company equals or exceeds the accumulated losses.

(*viii*) any amount of profits derived from the export of goods or merchandise to which section 80 HHC is applicable. **(This provision has been inserted with effect from 1998-99.)**

6. The provisions contained above shall not have any effect on unabsorbed.

TAX CREDIT IN RESPECT OF TAX PAID UNDER MAT [Section 115JAA]

1. In case any amount is paid u/s 115JA by a company for any assessment year, such company shall be allowed credit of amount of tax so paid in prescribed manner.
2. The tax credit to be allowed shall be an amount equal to difference between the amount of tax paid u/s 115JA and tax payable on his total income as computed under this Act.
3. No interest shall be allowed on the amount of tax credit to be given.
4. Amount of tax credit as determined above shall be allowed to be carried forward upto 4 assessment years succeeding the assessment year in which such credit became due.
5. Tax credit will be allowed in the year in which tax becomes payable on the total income as computed under this Act without applying the provisions of section 115JA.
6. In case the amount of tax credit allowed can be reduced or increased as per orders u/s 143(1), 147, 154, 155, 158, 245D(4), 250, 254, 260, 262, 263 or 264.

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SPECIAL PROVISIONS RELATING TO TAX ON DISTRIBUTED PROFITS [Section 115-O]

1. Tax on distributed profits of companies

In addition to income tax chargeable on the total income of a domestic company and such company has declared, distributed or paid some amount by way of dividends [whether interim or final] on or after 1.6.1997 whether out of current or accumulated profits, it shall have to pay additional income tax at the rate of 10% on amount of dividend so declared, distributed or paid. Such tax shall be known as tax on distributed profits.

2. Responsibility to deposit tax

The principal officer of such domestic shall be liable to deposit tax on distributed profits to the credit of Central Government within 14 days of the date of declaration of dividend.

3. Final payment

The amount of tax on distributed profits deposited as per above shall be considered as final and no further credit shall be claimed by such domestic company or any other person.

4. No deduction

The company or any shareholder of such company shall not have any right to claim any deduction for the amount of tax paid under this section.

With effect from assessment year 1998-99 following changes have been made in section 115 :

1. U/s 115A tax rates on royalty received for technical services rendered, are
   - (*a*) if agreement was entered on or before 31.5.1997—30%
   - (*b*) if agreement was entered after 31.5.1997—20%
2. Due to exemption of dividend from Indian companies u/s 10(33), the words "income from dividend" as given in section 115AC, 115AD and 115C have been replaced by income from "dividends other than dividend referred to in section 115-O".

QUESTIONS

1. Write notes on:
   - (*a*) Incomes on which no tax is payable;
   - (*b*) Tax on dividend received by a foreign company;
   - (*c*) Tax on capital gain on sale of Bonds purchased in foreign currency.
2. Write in brief the provisions relating to assessment of non-residents.

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7 PRESUMPTIVE ASSESSMENT FOR RETAIL TRADERS

Computation of income from retail trade—Eligible persons—Statement of turnover—Non filing of return—No deductions—No proceedings—Questions.

With a view to increase the tax revenue and to save the retail traders from undue hardship of assessment proceedings, the Finance Act 1992 has inserted this new chapter in Income-tax Act. For the time being this amendment has been made for a period of two years only *i.e. assessment year 1993-94 and 1994-95* (Previous year 1992-93 and 1993-94) but it has been further extended upto assessment year 1997-98.

1. Deemed Profit [Section 115 K (1)]

This section is applicable to a person who is

(*a*) Carrying on the business of retail trade in any goods or merchandise; or

(*b*) Carrying on the business of running on eating place or of operating, hiring or leasing a motor car, a maxicab or a three wheeled motor vehicle or any other business as may be prescribed; or

(*c*) Engaged in any vocation; and

Submits a statement prescribed u/s 115 K (4), a sum of Rs. 49,330 shall be deemed to be the profits and gains of such person.

2. Persons eligible for presumptive assessment [Section 115K(2)]

The provisions of this section are applicable to—

(*a*) an individual or HUF only;

(*b*) such person has not been assessed to income tax for any assessment year prior to and including 1992-93;

(*c*) such person has income derived from the business of retail trade and turnover from such trade during the previous year does not exceed Rs. 7 lacs. and his income from such business or vocation does not exceed Rs. 49,330.

(*d*) such person does not have any income chargeable to tax from any other source falling under any head of income except income from retail trade.

The person, must fulfil all the above conditions to qualify for presumptive assessment.

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3. Rates of Tax [Section 115 K (3)]

Any person to whom this section is applicable shall deposit tax at the rates specified in the Finance Act of the relevant year for computation of advance tax.

4. Statement of Turnover [Section 115 K(4)]

The persons who are eligible, as per above, have to submit a statement. Such statement must—

(*a*) be in the prescribed form and should contain
  (*i*) Name of such person;
  (*ii*) Address;
  (*iii*) Nature of business;
  (*iv*) Declaration by him that his turnover from such trade does not exceed Rs. 7,00,000; and
  (*v*) His income from such trade, business or vocation does not exceed Rs. 49,330.
  (*vi*) To be verified in prescribed manner.

(*b*) be submitted on or before 31st day of March of the relevant previous year;

(*c*) be accompanied by—proof of payment of tax (calculated in prescribed manner).

Calculation of tax

(*i*) Take Rs. 49,330 as total income of the year.

(*ii*) Apply the scheduled rates of tax on such calculated income and this is the amount of tax payable by such assessee.

Illustration 1. Mr. Devgan declares his turnover for the previous year 1996-97 as Rs. 7,00,000. Calculate the amount of tax payable by him and give the date by which he should deposit the amount of tax.

Solution

		Rs.
Turnover		7,00,000
Income	Rs. 49,330	
Tax on Rs. 49,330 at the rates applicable for assessment year 1997-98		
Rs. 40,000	Nil	Nil
Balance 9,330	15%	1,400
Tax Payable		Rs. 1,400

Tax is to be deposited by 15th March 1997.

5. Non-filing of Return [Section 115L]

Any person who has submitted a statement u/s 115K(1) shall not be required to furnish a return of income u/s 139(1) and provisions regarding assessment proceedings shall not be applicable.

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6. Disallowance of any deduction or rebate [Section 115M]

Any person who has submitted a statement u/s 115K(1) shall not be eligible to claim any deductions u/s 80 or any rebate of tax u/s 88.

7. No proceedings in certain cases [Section 115N]

No proceedings under any of the provisions of this Act shall be initiated against a person who has submitted a statement u/s 115K(1). In case of any additional evidence available only Deputy Commissioner of Income tax can initiate proceedings if he has reason to believe that the statement given is untrue.

QUESTIONS

1. What are the important provisions of the presumptive assessment of retail trader ?
2. Discuss the provisions of law relating to assessment of a retail trader u/s 115K ?

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PART V

ADMINISTRATION OF ACT

1. INCOME-TAX AUTHORITIES
2. PROCEDURE FOR ASSESSMENT
3. COLLECTION OF TAX
4. RECOVERY OF TAX AND REFUNDS
5. SETTLEMENT COMMISSION
6. APPEALS AND REVISIONS
7. PENALTIES AND PROSECUTIONS

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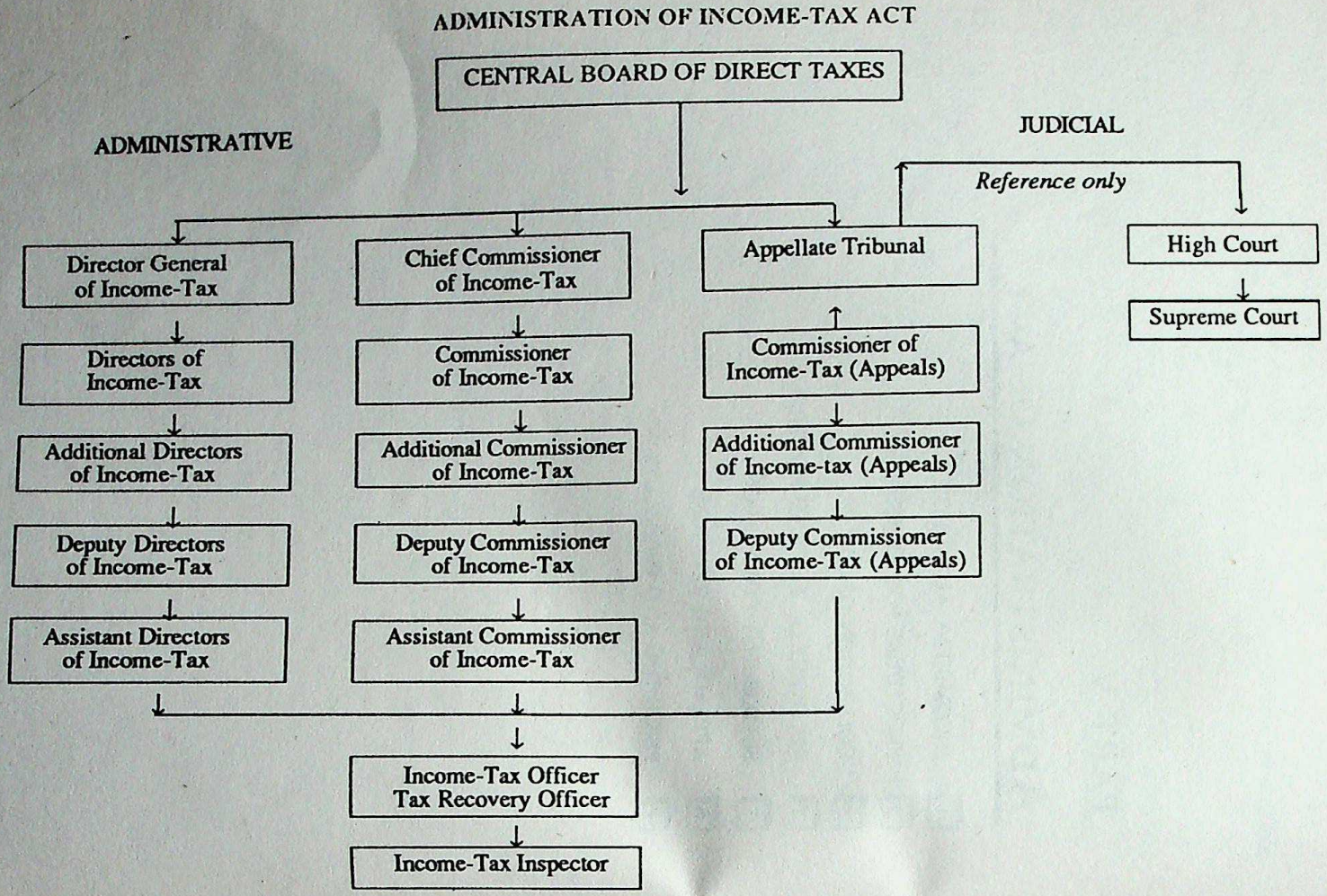

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1 INCOME TAX AUTHORITIES

Various Authorities—Central Board of Direct Taxes—Powers—Director General of Income-Tax—Powers—Chief Commissioner of Income-tax—Powers—Assessing Officer—Appointment—Jurisdiction—Powers—Powers relating to search and seizure—Settlement Commission—Questions.

VARIOUS AUTHORITIES

Section 116 of the Income-Tax Act, 1961 provides for the administrative and judicial authorities for administration of this Act. The Direct Tax Laws (Amendment) Act, 1987 has brought far-reaching changes in the organisational structure. The implementation of the Act lies in the hands of these authorities. The change in designation of certain authorities and creation of certain new posts in the structure are the main features of amendments made by The Direct Tax Laws (Amendment) Act, 1987. The new structure of authorities has been properly depicted in a chart on the facing page. These authorities have been grouped into two main wings :

(i) Administrative

Under this wing authorities are :

(*i*) The Central Board of Direct Taxes

(*ii*) Director Generals of Income-tax/Chief Commissioner of Income-tax

(*iii*) Directors of Income-tax/Commissioners of Income-tax/Commissioner of Income-tax (Appeals)

(*iv*) Additional Directors of Income-tax, or Additional Commissioners of Income-tax or Addiitonal Commissioners of Income-tax (Appeal) [*Inserted by Finance Act 1994*]

(*v*) Deputy Directors of Income-tax/Deputy Commissioners of Income-tax/ Deputy Commissioners of Income-tax (Appeals)

(*vi*) Assistant Directors of Income-tax/Assistant Commissioner of Income-tax

(*vii*) Income-tax Officers

(*viii*) Tax Recovery Officers

(*ix*) Inspectors of Income-Tax

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(ii) Assessing Officer [Section 2(7A)]

It means the Assistant Commissioner or the Income-tax Officer who is vested with relevant Jurisdiction u/s 120 (1) or 120 (2) or any other provisions of this Act. It also includes the Deputy Commissioner who is directed u/s 120 (4) (b) of this Act to act as Assessing Officer.

Importance of Assessing Officer

In the organisational set-up of the income tax department Assessing Officer plays a very vital role. He is the primary authority who initiates the proceedings and is directly connected with the public. Form the time of filing of return till the assessment is completed he plays a pivotal role. He can start proceedings for non filing of return, imposition of penalties etc. Orders passed by him can be challenged only on appeal. The department can revise his orders only if it is proved that these are prejudicial to the revenue and that too only by the Commissioner of Income tax.

(iii) Appointment of Income-tax authorities [Section 117]

(*a*) *Power of Central Government.* The Central Government may appoint such persons as it thinks fit to be income-tax authorities. It kept with itself the powers to appoint authorities upto and above the rank of an Assistant Commissioner of Income-tax [Section 117 (1)].

(*b*) *Powers of the Board and other higher authorities.* Subject to rules and regulations of the Central Government regarding the conditions of service of persons in public services, the Central Govt. has authorised the Board, or a Director General, a Chief Commissioner, a Commissioner or a Director to appoint income-tax authorities below the rank of Assistant Commissioner. [Section 117 (2)].

(*c*) *Powers to appoint executive and ministerial staff.* U/s 117 (3) the Board has been empowered to appoint such executive or ministerial staff as may be necessary to assist the income-tax authorities in the execution of their functions.

(iv) Control of Income-tax authorities [Section 118]

The income-tax authorities will be subordinate to such authorities as may be prescribed in a notification to be issued by the Board in this behalf.

1. CENTRAL BOARD OF DIRECT TAXES

In the administrative set up of the Income-tax department highest authority is the Central Board of Direct Taxes, constituted under the provisions of Central Board of Revenue Act, 1963. The Board functions under the control of Ministry of Finance, Government of India. Its jurisdiction is whole of India.

The Central Government is empowered to appoint its members and the Government can increase the number upto a maximum of five. At present there are four members besides the Chairman. One of the members of the Board is appointed as its Chairman.

Powers. The whole of income-tax department is to be looked after by the Board. It has to perform the functions of administration, supervision and control of

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entire Income-tax structure in India. The orders and directions issued by the Board are to be complied with by all the subordinate authorities. The orders and directions issued by the Board will not interfere in the performance of appellate functions of Appellate Commissioner.

The Income-tax Act provides following specific *powers* to the Board :

(*i*) The Board can declare any association whether incorporated or not and whether Indian, or Non-Indian, as company under the provision of Section 2(17).

(*ii*) The Board has power to determine the jurisdiction of various authorities mentioned in this Act. [Section 118].

(*iii*) The Board may issue directions for the exercise of powers and performance of the functions by all or any of these authorities. While issuing such directions the Board will keep in mind any of the following criteria :

(*a*) territorial area;

(*b*) persons or classes of persons;

(*c*) incomes or classes of incomes; and

(*d*) cases or classes of cases. [Section 120 (1) and (3)].

(*iv*) The Board may authorise, by general or specific order, Director General or Director to perform the powers of any of the income-tax authorities. [Section 120].

(*v*) The Board may empower Director General or Chief Commissioner or Commissioner to authorise Deputy Commissioner or Deputy Director to exercise the powers of assessing authority in respect of any specified area, person, incomes or cases or class of persons, class of incomes or class of cases. [Section 120 (4)].

(*vi*) The Board may authorise any of the authorities to exercise its powers concurrently with any other authority. In case such notification is issued by the Board, the lower authority (in rank) shall exercise such powers as are directed to it by higher authority. [Section 120 (5)].

(*vii*) To carry out the different provisions of the Act the Board makes rules for whole of India. [Section 295].

(*viii*) The Central Board of Direct Taxes has been empowered by Taxation Laws (Amendment) Act 1975 to make rules regarding the maintenance of accounts and documents required under Section 44 AA. It is obligatory for professionals to maintain such books and documents as may enable the Assessing Officer to compute his total income.

The Board has the power to make rules and issue orders, instructions, directions etc., to all the persons employed for the proper and efficient administration of the Act, but the Board cannot issue orders, directions etc. of the following nature :

(*a*) To require any income-tax authority to make a particular assessment or to dispose of a particular case in a particular manner.

(*b*) To interfere with the discretion of the *Deputy Commissioner of Income-tax (Appeals)* in the exercise of his appellate functions. *Sirpur Paper Mill Ltd. v. CWT 77 ITR 6 (SC) and J.L. Synthetics Ltd. V. CBDT 83 ITR 335 (SC).*

(*ix*) Section 119 (2) empowers the Board to issue general or special circulars or orders which are not prejudicial to assessees and Board feels that these are necessary

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or expedient for the purpose or proper and efficient management of the work of assessment and collection of revenue. Section 119 (2) (*b*) says that to avoid genuine hardship in any case or class of cases, the Board, if it thinks desirable can authorise any income-tax authority not being a Deputy Commissioner (Appeal) or Commissioner (Appeals) or to admit an application or claim for any exemption, deduction, refund or any relief under this Act after the expiry of specified period fixed for such an application, claim etc. The Supreme Court has also held the validity and binding nature of such type of circulars which are beneficial to the assessee and the tax-payer has right to get them enforced in a court. *(Navnital Javeri v. Sen, 56 ITR 198, 203).*

If any circular beneficial to the assessee is subsequently withdrawn, such a withdrawal cannot affect the validity of the action already taken pursuant to it. *(Tata Iron & Steel Co. Ltd. v. Upadhaya, 96 ITR 115).*

(*x*) To avoid undue hardship in any case or class of cases, the Board may relax any of the requirements given under the chapters of Aggregation, Carry Forward and set off of losses or Deductions u/s 80 of the Act. Such relaxation has to be provided in general or special order to be issued by the Board for reason to be specified therein. Such relaxation may relate to failure of the assessee to comply with any of the requirements regarding claim of deduction subject to following conditions:

(*i*) The default of the assessee was due to circumstances beyond the control of assessee; and

(*ii*) Assessee has complied with such requirements before the completion of assessment is relation to the previous year in which such deduction is claimed. However each such order is to be placed before each house of parliament.

2. DIRECTOR GENERAL/CHIEF COMMISSIONER OF INCOME-TAX

(*i*) *Appointment.* The Central Government may appoint such persons as it thinks fit to be the Director General/Chief Commissioner of Income-tax.

(*ii*) *Jurisdiction.* The jurisdiction of these authorities shall be determined by the C.B.D.T. keeping in view the area, persons, incomes or cases.

(*iii*) *Function.* The C.B.D.T. may by general or special order and subject to such conditions, restrictions or limitations, authorise any Director or Chief Commissioner to perform such functions of any other income-tax authority as may be assigned to him in such order.

(*iv*) *Powers*

(*a*) The Director General or Chief Commissioner may be empowered to authorise a Deputy Commissioner to exercise the powers of an Assessing Officer in respect of a person, case, income or an area.

(*b*) These authorities may be empowered by the Board to appoint income-tax authorities below the rank of an Assistant Commissioner.

(*c*) These authorities may, after giving the assessee a reasonable opportunity of being heard in the matter, and after recording his reasons, transfer the case from one Assessing Officer subordinate to him.

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(*d*) The Director General or Director or any other officer so authorised, may exercise the powers of Assessing Officer, in case he has reason to suspect that any income has been concealed or is likely to be concealed by an assessee coming within his jurisdiction.

(*e*) Section 119 (3) empowers the Director to issue instructions to the Assessing Officers and such instructions are issued for their guidance and are binding on them.

(*f*) Taxation Laws (Amendment) Act, 1975 has given the power to the Director to make any inquiry or investigation in case of such type of assessees who falls within his jurisdiction and in whose case he has reason to suspect that any income has been concealed or is likely to be concealed. This section also confers on the Director such powers which are vested in a court under the Code of Civil Procedure, 1908.

(*g*) The Director shall be competent to make any inquiry under this Act and for this purpose shall have all the powers that an Assessing Officer has under this Act in relation to the making of inquiries. [Section 135].

Powers conferred on the Director under Section 132 (1), 132-A have been explained under the heading 'Search and Seizure'.

3. COMMISSIONER/DIRECTORS/ADDITIONAL COMMISSIONER/ADDITIONAL DIRECTORS OF INCOME-TAX

(*i*) *Appointment.* The Central Government may appoint such persons as it thinks fit to be the Commissioners of Income-tax.

(*ii*) *Jurisidiction.* The jurisdiction of Commissioners is to be determined by the Central Board of Direct Taxes keeping in view the area, persons, incomes or cases.

(*iii*) *Functions.* The Board may, by general or specific order and subject to such conditions, restrictions or limitations, authorise any commissioner to perform such functions of any other income tax authority as may be assigned to him in such order.

(*iv*) *Powers*

(*a*) Under the directions of the Board, a Commissioner may exercise the powers of an Assessing Officer.

(*b*) A Commissioner has the power to transfer any case from one or more Assessing Officers subordinate to him to any other Assessing Officer or Officers also subordinate to him. He can do so only after giving the assessee an opportunity of being heard and after recording the reasons for doing so.

(*c*) The Commissioner has been empowered to grant approval for an order issued by the Assessing Officer asking a non-company assessee to get its accounts audited from a Chartered Accountant. [Section 142 (2A)].

(*d*) The prior approval of the Commissioner is required for reopening of an assessment [Section 147] beyond the time limit of 4 years.

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(*e*) The Commissioner has the power to revise an order passed by Assessing Officer, if in his opinion it is erroneous or prejudicial to the interests of the revenue. He can do so only after giving the assessee an opportunity of being heard. [Section 263].

(*f*) The Commission has the power to revise any other order issued by I.T.O. and not covered under section 263, either of his own motion or on application by the assessee for such revision. [Section 264].

(*g*) The Commissioner may direct the Assessing Officer to appeal to Appellate Tribunal against the order passed by Commissioner (Appeals). [Section 253 (2)].

4. DEPUTY COMMISSIONERS AND ASSISTANT COMMISSIONERS OF INCOME TAX

(*i*) *Appointment.* The Central Govt. appoints Deputy and Assistant Commissioners of Income-tax and are subordinate to Commissioners, and Chief Commissioners.

(*ii*) *Jurisdiction.* The area of operation is specified by the Board or any other authority so authorised. Their jurisdiction can be concurrent with other such authorities.

(*iii*) *Functions.* They perform such functions as are assigned to them by general or specific order issued by the Board and in respect of specific area, class of persons or specific cases or class of cases.

(*iv*) *Powers :*

(*a*) He is empowered to accord sanction to levy additional income-tax on companies in which public are not substantially interested. [Section 107].

(*b*) He may be authorised by the Board, or Chief Commissioner to exercise the powers of assessing officer.

(*c*) He has the power to cancel the registration of a firm which is not a genuine firm. [Section 186 (1)].

(*d*) He has the power to issue instructions to Assessing Officer to revise an order issued by I.T.O. if he has received an application from assessee regarding a pending case. [Section 144 A].

5. ASSESSING OFFICER (ASSISTANT COMMISSIONER/INCOME TAX OFFICER)

The Assessing Officer is the most important authority in the organisation structure of Income-tax department. He is the primary authority to initiate assessment proceedings and make assessment. He is the only authority to collect tax. He is the authority which comes into contact with the public.

Jurisdiction

1. Determination of CBDT. The jurisdiction of income-tax authorities shall be determined by the Central Board of Direct taxes. While determining the jurisdiction the Board may consider the following :

(*i*) Territorial area,

(*ii*) Persons or classes of persons,

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(*iii*) Incomes or classes of incomes,

(*iv*) Cases or classes of cases.

2. Instructions by Director General/Chief Commissioner or Commissioner of Income-tax. The Assessing Officer shall perform his functions in respect of such area or such classes of persons or incomes as the above mentioned authorities may instruct. The Assessing Officer shall have jurisdiction within the area assigned to him and in respect of :-

(*i*) Any persons who is carrying on his business or profession in such area, or if he is carrying on business at more than one place, the principal place of business is situated within such area; and

(*ii*) Any other persons who is residing in such area.

3. Concurrent Jurisdiction. If two or more persons are appointed as Assessing Officers in same area, each one will perform such functions as are directed by the Commissioner. If two or more Assessing Officers are required to attend the cases in same area, the directions of that Assessing Officer who is senior in rank shall prevail.

4. Dispute Regarding Jurisdiction. (*i*) If there is dispute regarding the jurisdiction of an Assessing Officer, it will be decided by the Director/Chief Commissioner or Commissioner of Income-tax.

(*ii*) If dispute relates to areas which fall within the jurisdiction of different such authorities, it will be decided by the concerned Director General or Chief Commissioner or Commissioner.

(*iii*) If such authorities are not in agreement the dispute will be decided by the Board or any other authority so notified.

5. Jurisdiction not to be Disputed. (*i*) The jurisdiction of the Assessing Officer shall not be challenged after the expiry of one month from the date on which he has filed a return u/s 139(1) or after the completion of assessment whichever is earlier.

(*ii*) If he has not filed such return and the time allowed by notice served under sections 142(1) or 148 or 144 (first provision) has expired.

(*iii*) If Assessing Officer is not satisfied about the contentions of the assessee regarding the dispute, he will refer the case for decision to the Commissioner/Chief Commissioner or Director General of Income-tax.

Powers

The Assessing Officer shall exercise the following powers:-

I. **Power of Civil Court.** These authorities shall have the same powers, as are vested in a court under the Code of Civil Procedure 1908, when trying a suit in respect of the following matters:

(*i*) Discovery and Inspection;

(*ii*) Enforcing the attendance of any person and examining him under oath;

(*iii*) Compelling a person to produce books of accounts and other documents; and

(*iv*) Issuing commissions. [Section 131]

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II. **Powers of Search and Seizure.** These authorities shall have the power of searching any building, place, vessel, vehicle or aircraft and seize books of accounts, other documents, money, bullion, jewellery or other valuable articles or things. Identification marks shall be put on the seized articles and an inventory shall be made. [Section 132].

The books of accounts or the other documents seized *shall not be retained* by the authorities for a period exceeding 180 days from the date of seizure unless for the reasons recorded, the approval of Chief Commissioner or Commissioner, is obtained. The extension cannot be granted beyond 30 days in case of books relating to the year to which they are relevant. [Section 132(8)].

The assets so seized shall be retained by the Assessing Officer in his authority and shall be applied towards the recovery of existing and estimated tax liability of the assessee.

III. **Power of Assessment.** An Assessing Officer or any other authority acting as Assessing Officer shall have following *powers* while performing his functions:

(*i*) Power regarding self-assessment as mentioned in Section 140A.

(*ii*) Power of making regular assessment under Section 143 and Best judgment assessment under Section 144.

(*iii*) Power to reopen an assessment under Section 146.

(*iv*) Power to reopen an assessment in case income has escaped assessment under Sections 147 and 148.

(*v*) Power to treat a person as an agent under Section 163.

(*vi*) Power to assess a person leaving India under Section 174 and income of person trying to alienate his assets under Section 175.

IV. **Power to call for information.** The aforesaid authorities have the power to call for necessary information from a firm and H.U.F.

They can ask an assessee to furnish a statement of names and addresses of all the persons to whom he has paid in any previous year rent, interest, commission, royalty or brokerage etc. amounting to more than Rs. 1,000 or such higher amount as may be prescribed together with particulars of all such payments. The Assessing Officer can ask any person including a banking company or an officer thereof to furnish information relating to such points or matters or to furnish statements of accounts and affairs verified in the prescribed manner. [Section 133].

V. **Power of Survey.** Under Section 133A, an Income-tax authority may enter any place where business or profession is carried on, if such place is within the limits of the area assigned to him or is occupied by any person in respect of whom the Assessing Officer exercises jurisdiction.[Section 133A].

The Income-Tax authority may require the person attending the business or profession to afford necessary facilities to inspect books of accounts or documents, and to check and verify the cash, stocks or other valuables which may be available at the place. [133A (1)]. The Income-tax authority may enter any place only after sunrise and before sunset. [133A (2)]. No books of accounts, documents or cash, stock or valuable shall be removed from the place where such authority has entered. [133A(4)]. The Income-tax authority may ask a person to submit the necessary

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information relating to expenditure incurred in a particular ceremony or event. [133A(5)]. These powers may also be exercised by the Director General, the Chief Commissioner, the Director and the Commissioner.

VI. **Power to Inspect Registers of Companies.** [Section 134]. The above-mentioned authority, may inspect, if necessary, take copies or cause copies to be taken of any register of members, debentureholders, mortgagees of company or of any entry in such register.

6. INCOME TAX INSPECTOR

They are appointed by Chief Commissioner or Commissioner of Income-tax and are subordinate to Assessing Officers. They assist Assessing Officers in performance of their duties. They may be directed to perform any other function by general or specific order.

All the proceedings under this Act conducted before an Income-tax authority shall be deemed to be judicial proceedings within the meanings of Sections 193 and 228 and for the purposes of Section 196 of the Indian Penal Code. [Section 136].

POWERS OF INCOME TAX AUTHORITIES RELATING TO SEARCH AND SEIZURE [Section 132]

Entering and Searching the Premises

Where the Director General or Director or the Chief Commissioner or the Commissioner or any such Deputy Director or Deputy Commissioner has been empowered in this behalf by the Board, in consequence of information in his possession, has reason to believe that:

(*a*) any person to whom summons under sub-section (1) of Section 131 of this Act, or under sub-section (1) of Section 142 of this Act were issued to produce, or cause to be produced, any books of account or other documents, has omitted or failed to produce or cause to be produced, such books of accounts, or other documents as required by such summons or notices; or

(*b*) any person to whom summons or notice as aforesaid has been or might be issued will not, or would not, produce or cause to be produced, any books of accounts or other documents which will be useful for, or relevant to any proceeding under the Indian Income-tax Act;

(*c*) any person is in possession of any money, bullion, jewellery or other valuable article or thing and such money, bullion, jewellery or other valuable article or thing represents either wholly or partly income or property *which has not been, or would not be, disclosed* for the purpose of the Indian Income-tax Act.

Then,—

(A) The Director General or Director or the Chief Commissioner or the Commissioner, as the case may be, may authorise any Deputy Director, Deputy Commissioner, Assistant Director, Assistant Commissioner or Assessing Officer; or

(B) Such Deputy Director or Deputy Commissioner as the case may be, may authorise any Assistant Commissioner or Assistant Director or I.T.O.

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(the officer so authorised in all cases being hereinafter referred to as the authorised officer) to—

(*i*) enter and search any *building, place, vessel or aircraft* where he had reason to suspect that such books of accounts, other documents, money, bullion, jewellery or other valuable articles or things are kept;

(*ii*) break open the lock of any door, box, locker, safe, almirah or other receptacle exercising the powers conferred by clause (i) where the keys thereof are not available;

(*iii*) search any person who has got out of, or is about to get into, or is in the building, place, vessel, vehicle or aircraft, if the authorised officer has reason to suspect that such person has secreted about his person any such books of account, other documents, money, bullion, jewellery or other valuable article or thing;

(*iv*) seize any such books of account, other document, money, bullion, jewellery or other valuable article or thing found as a result of such search;

(*v*) place marks of identification on any books of accounts or other documents or make or cause to be made extract or copies thereof;

(*vi*) make a note or an inventory any such money, bullion, jewellery or other valuable article or thing.

Provided that where any building, place, vessel, vehicle or aircraft referred to in clause (*i*) is within the area or jurisdiction of any Chief Commissioner, but such Commissioner has no jurisdiction over the person referred to in clause (*a*) or clause (*b*) or clause (*c*), then it shall be competent for him to exercise the power under this sub-section in all cases where he has reasons to believe that any delay in getting the authorisation from the Chief Commissioner having jurisdiction over such person may be prejudicial to the interests of the revenue [Section 132(1)].

The Finance Act, 1988 has further provided that where it is not possible or practicable to take physical possession of any valuable article or thing and remove it to a safe place due to its volume, weight or other physical characteristics or due to its being of a dangerous nature, the authorised officer may serve an order on the owner or the person who is in immediate possession or control thereof that he shall not remove, part with or otherwise deal with it except with the previous permission of such authorised officer.

Premises in the Jurisdiction of another Officer [Section 132 (1A)]

Where any Chief Commissioner, in consequence of information in his possession, has reason to suspect that any books of account, other documents, money, bullion, jewellery or other valuable article or thing in respect of which an officer has been authorised by the Director General or Director or any other Chief Commissioner or any such Deputy Director or Deputy Commissioner or Assistant Commissioner as may be empowered in this behalf by the Board to take action under clauses (*i*) to (*v*) of sub-section (1) are or is kept in any building, place, vessel or aircraft not mentioned in the authorisation under sub-section (1), such Chief Commissioner may, notwithstanding anything contained in Section 120 authorise the said officer to take action under any of the clauses aforesaid in respect of such building, place, vessel, vehicle or aircraft.

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Requisitioning the Police Help [Section 132 (2)]

The authorised officer may requisition the service of any police officer or of any officer of the Central Government, or of both to assist him for all or any of the purpose specified in sub-section (1) or sub-section (1A) and it shall be the duty of every such officer to comply with such requisition.

Ordering Non Removal of Assets [Section 132 (3)]

The authorised officer may, where it is not practicable to seize any such books of account, other documents, money, bullion, jewellery or other valuable article or thing, serve an order on the owner or the person who is in immediate possession or control thereof that he shall not remove, part with or otherwise deal with except with the previous permission of such officer and such officer may take such steps as may be necessary for ensuring compliance with this sub-section.

Administering Oath [Section 132 (4)]

The authorised officer may, during the course of the search or seizure, examine on oath any person who is found to be in possession or control of any books of account, documents, money, bullion, jewellery or other valuable article or thing and any statement made by such person during such examination may thereafter be used in evidence in any proceeding under the Indian Income-tax Act.

Explanation. For the removal of doubts, it is hereby declared that the examination of any person under this sub-section may be not merely in respect of any books of account, other documents or assets found as a result of the search, but also in respect of all matters relevant for the purposes of any investigation connected with any proceeding under the Indian Income-tax Act.

Ownership of Seized Books [Section 132 (4A)]

Where any books of account, other documents, money, bullion, jewellery or other valuable articles or things are or is found in the possession or control of any person in the course of search, it may be presumed—

(*i*) that such books of account, other documents, money, bullion, jewellery or other valuable articles or things belongs to such person;

(*ii*) that the contents of such books of account and other document are true; and

(*iii*) that the signature and every other part of such books of account and other documents which purport to be in the handwriting of any particular person or which may reasonably be assumed to have been signed by, or to be in the handwriting, and in the case of a document stamped, executed or attested, that it was duly stamped and executed or attested by the person by whom it purports to have been so executed or attested.

Levying of Tax [Section 132(5)]

Where any money, bullion, jewellery or other valuable article or thing (hereinafter in this section and section 132 A and 132 B referred to as the assets) is seized under sub-section (1) or sub-section (1A), as a result of a search initiated or requisition made before the first day of July 1995, the Assessing Officer, after

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affording a reasonable opportunity to the person concerned for being heard and making such enquiry as may be prescribed shall, within 120 days of the seizure, make an order, with the previous approval of the Deputy Commissioner,

(*i*) estimating the undisclosed income (including the income from the undisclosed property) in a summary manner to the best of his judgment on the basis of such materials as are available with him;

(*ii*) calculating the amount of tax on the income so estimated in accordance with the provisions of the Indian Income-tax Act;

(*iii*) determining the amount of interest payable and the amount of penalty imposable in accordance with the provisions of the Indian Income-tax Act, as if the order had been the order of regular assessment;

(*iv*) specifying the amount that will be required to satisfy any existing liability under this Act and any one or more of the Acts specified in clause (*a*) of sub-section (1) of section 230A in respect of which such person is in default or is deemed to be in default,

and retain in his custody such assets or part thereof as are in his opinion sufficient to satisfy the aggregate of the amount referred to in clauses (*ii*), (*iia*) and (*iii*) and forthwith release the remaining portion, if any, of the assets to the person from whose custody they were seized.

Provided that if, after taking into account the material available with him, the Assessing Officer is of the view that it is not possible to ascertain to which particular previous year or years such income or any part thereof relates, he may calculate the tax on such income or part as the case may be, as if such income or part were the total income chargeable to tax at the rates in force in the financial year in which the assets were seized and may also determine the interest or penalty, if any, payable or imposable accordingly.

Provided further that where a person has paid or made satisfactory arrangement for payment of all the amounts referred to in clauses (*ii*), (*iia*) and (*iii*) or any part thereof, the Assessing Officer may, with the previous approval of the Chief Commissioner/Commissioner, release the assets or such part thereof as he may deem fit in the circumstances of the case.

Rules regarding retention of seized books and documents

1. If the Assessing Officer is satisfied that the seized assets or any part thereof were held by such person for or on behalf of any other person, the Assessing Officer may proceed under sub-section (5) against such other person, and all the provisions of this section shall apply accordingly.

2. The books of account or other document shall not be retained by the authorised officer for a period exceeding one hundred and eighty days from the date of the seizure unless the reason for retaining the same are recorded by him in writing and the approval of the Chief Commissioner/Director General/Commissioner/Director for such retentions is obtained;

Provided that the Chief Commissioner/Director General/Commissioner/ Director shall not authorise the retention of the books of account and other documents for a period exceeding thirty days after all the proceedings under the Indian Income-tax Act, in respect of the years for which the books of account or other relevant documents are completed.

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3. The person from whose custody the books of account or other documents are seized may make copies thereof, or take extracts therefrom, in the presence of the authorised officer or any other person empowered by him in this behalf, at such place and time as the authorised officer may appoint in this behalf.

4. Where the authorised officer has no jurisdiction over the person, the books of account or other documents or assets seized under that sub-section shall be handed over by the authorised officer to the Assessing Officer having jurisdiction over such person within a period of fifteen days of such seizure and thereupon the powers exercisable by the authorised officer under sub-section (8) or sub-section (9) shall be exercisable by such Assessing Officer.

5. If a person legally entitled to the books of account or other documents seized objects for any reason to the approval by the Chief Commissioner under sub-section (8), he may make an application to the Board stating therein the reasons for such objection and requesting for the return of the books of account or other documents [132(10)].

6. If any person objects for, any reason, to an order made under sub-section (5) he may, within thirty days of the date of such order, make an application to such Chief Commissioner or Commissioner stating therein the reasons for such objection and requesting for appropriated relief in the matter [132(11)].

(6A) In case any application was pending with any other authority, it stands automatically transferred to the Commissioner with effect from 1-10-1984. The Commissioner may proceed with such application from the stage at which it was left. [132(11)] *[Inserted by Taxation Laws (Amendment) Act, 1984].*

7. On receipt of the application under sub-section (10) the Board, or on receipt of application under sub-section (11) the Commissioner may, after giving the applicant an opportunity of being heard, pass such order as it thinks fit.

8. The provisions of the Code of Criminal Procedure, 1973 relating to searches and seizure shall apply, so far as may be, to searches and seizure.

9. The Board may make rules in relation to any search or seizure under this section, in particular and without prejudice to the generality of the foregoing power. Such rules may provide for the procedure to be followed by the authorised officer—

(*i*) for obtaining ingress into any building, place, vessel, vehicle or aircraft to be searched where free ingress hereto is not available;

(*ii*) for ensuring safe custody of any books of account or other documents or assets seized.

Explanation 1: In computing the period for the purposes of sub-section (5), any period during which any proceeding under this section is stayed by an order or injuction of any court shall be excluded.

Explanation 2: In this section, the word "proceeding" means any proceeding in respect of any year, whether under the Indian Income-tax Act, which may be pending on the date on which a search is authorised under this section or which may have been completed on or before such date and includes also all proceedings under this Act which may be commenced after such date in respect of any year.

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Requisitioning of Books of Account [Section 132 (A)]

1. Where the Director General or the Director or the Chief Commissioner or the Commissioner, in consequence of information in his possession, has reason to believe that—

(*a*) any books of account or other documents will be useful under sub-section (1) of section 131 of this Act; or under sub-section (1) of section 142 of this Act and a notice was issued to produce, or cause to be produced, any books of account or other documents, has omitted or failed to produce, or cause to be produced, such books of account or other documents as required by such summons or notice and the said books of account or other documents have been taken into custody by any officer or authority under any other law for the time being in force, or

(*b*) any books of account or other documents will be useful for, or relevant to, any proceedings under the Indian Income-tax Act, and any person to whom a summon or notice as aforesaid has been or might be issued will not, or would not, produce or cause to be produced, such books of account or other documents on the return of such books of account or other documents by any officer or authority by whom or by which such books of account or other documents have been taken into custody under any other law for the time being in force, or

(*c*) any assets represent either wholly or partly income or property which has not been, or would not have been disclosed for the purposes of the Indian Income-tax Act by any person from whose possession or control such assets have been taken into custody by any officer or authority under any other law for the time being in force, then, the Director General or the Director or the Chief Commissioner or the Commissioner may authorise any Deputy Director, Deputy Commissioner, Assistant Director, Assistant Commissioner or Income-tax Officer [hereafter in this section and in sub-section (2) of Section 278 D referred to as the requisitioning officer] to require the officer or authority referred to in clause (*a*) or clause (*b*) or clause (*c*), as the case may be, to deliver such books of account, other documents or assets to the requisitioning officer.

2. On a requisition being made under sub-section (1), the officer or authority shall deliver the books of account, or other documents or assets to the requisitioning officer either forthwith when such officer or authority is of the opinion that it is no longer necessary to retain the same in his or its custody.

3. Where any books of account, other documents or assets have been delivered to the requisitioning officer, the provisions of sub-section [(4A) to (14) both inclusive] of Section 132 and Section 133 B shall, so far as may be, apply as if such books of account, other documents or assets had been seized under sub-section (1) of Section 132 by the requisitioning officer from the custody of the person referred to in clause (*a*) or clause (*c*).

Application of Seized and Retained Assets [Section 132(B)]

1. The assets retained under sub-section (5) of Section 132 may be dealt with in the following manner, namely:—

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(*i*) The amount of the existing liability referred to in clause (*iii*) of the sub-section and the amount of the liability determined on completion of the regular assessment or re-assessment for all the assessment years relevant to the previous years to which the income referred to in clause (*i*) of that sub-section relates (including any penalty levied or interest payable) in connection with such assessment or re-assessment and in respect of which he is in default or is deemed to be in default may be recovered out of such assets.

(*ii*) If the assets consist solely of money, or partly of money and partly of other assets, the Income-tax Officer may apply such money in the discharge of the liabilities referred to in clause (*i*) and the assessee shall be discharged of such liability to the extent of the money so applied.

(*iii*) The assets other than money may also be applied for the discharge of any such liability referred to in clause (*i*) as remains undischarged and for this purpose such assets shall be deemed to be under distraint as if such distraint was effected by the Income-tax Officer under authorisation from the Chief Commissioner or the Commissioner under sub-section (5) of Section 226 and the Assessing Officer or Tax Recovery Officer may recover the amount of such liabilities by the sale of such assets and such sale shall be effected in the manner laid down in the Third Schedule.

2. Nothing contained in sub-section (1) shall preclude the recovery of the amount of liabilities aforesaid by any other mode laid down in this Act.

3. Any assets or proceeds thereof which remain after the liabilities referred to in clause (*i*) of sub-section (1) are discharged shall be forthwith made over or paid to the persons from whose custody the assets were seized.

4. (*a*) The Central Government shall pay simple interest at the rate of 15% per annum on the amount by which the aggregate of money retained under Section 132 and of the proceeds, if any, of the assets sold towards the discharge of the existing liability referred to in clause (*iii*) of sub-section (5) of that section exceeds the aggregate of the amounts required to meet the liabilities referred to in clause (*i*) of sub-section (1) of this section.

(*b*) Such interest shall run from the date immediately following the expiry of the period of six months from the date of the order under sub-section (5) of Section 132 to the date of the regular assessment or re-assessment referred to in clause (*i*) of sub-section (1) or as the case may be, to the date of last of such assessments or reassessments.

Power to call for information [Section 133]

The Assessing Officer, the Deputy Commissioner (Appeals), the Deputy Commissioner or the Commissioner may for the purposes of this Act call for following information :-

(*i*) Require any firm to furnish names and addresses of all the partners and their respective shares,

(*ii*) Require any HUF to furnish names and addresses of the manager and members of the family,

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(*iii*) Require any person who he has reason to believe to be a trustee, guardian or agent to furnish names and addresses of the persons for whom such person is acting as trustee or guardian or agent,

(*iv*) Require any person to give a statement of the names and addresses of all those persons to whom any amount exceeding Rs. 1,000 or any other amount so prescribed is paid as royalty, rent, interest, commission or brokerage or any annuity (not taxable under the head Salary) alongwith all particulars of amount so paid.

(*v*) Require any dealer or agent or any person concerned in management of stock or commodity exchange to furnish the names and addresses of all those persons to whom any payment has been made or from whom any payment has been received for sale, purchase or exchange of any asset alongwith particulars of any payment made,

(*vi*) Require any person including a banking company or any officer to furnish information in relation to such points or matters or to furnish statement of accounts and affairs verified in prescribed manner.

Powers under this clause may also be exercised by the Director General, Chief Commissioner, the Director or the Commissioner. In case no proceedings are pending powers under this section shall not be exercised by any officer below the rank of Director or Commissioner without the prior approval of the Director or the Commissioner.

Power of Survey [Section 133A]

Any Assessing Officer or his duly authorised inspector, Deputy Commissioner or Assistant Director has the power to enter:

(*i*) any place within the area of his jurisdiction; or

(*ii*) any place which is occupied by a person on whom he can exercise his jurisdiction and where such person is carrying on his business or profession; or

(*iii*) any place in respect of which he is authorised for the purposes of this section by such income-tax authority who is assigned the area within which such place is situated or who exercises jurisdiction in respect of any person occupying such place.

It may require the proprietor or any other person attending to such business or profession to afford him necessary facilities:

(*i*) to inspect books or accounts or other documents;

(*ii*) to verify and make an inventory of cash, stock;

(*iii*) to record the statements (which can help him to conduct the relevent proceedings under this Act) of any person.

In case the income-tax authority is not provided with such facility, such authority can proceed under section 131(1) and 131(2) against the proprietor or any other person attending to such business.

Provisions relating to Power to collect certain information [Section 133B]

The Finance Act, 1986 inserted a new Section 133 B in the Income-tax Act. Under the proposed provisions, the Income-tax authority will be empowered to enter

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any building or place within its jurisdiction or any building or place which is occupied by any person in respect of whom such authority exercises jurisdiction for the purposes of collection of any information which may be useful for or relevant to the purposes of the Act. Such authority shall require any person who is the occupant of the building or place to furnish such information as may be prescribed by rules made under this Act.

This new provision provides for entry of the Income-tax authority into a building or place where business or profession is carried on only during the time when it is open for the conduct of business or profession and in respect of any other place after sunrise and before sunset. Such authority shall have no power to remove or cause to be removed from the building or place, wherein it has entered any books of accounts or other documents or any cash, stock or other valuable articles or things.

"Income-tax Authority" means a Deputy Commissioner, an Assistant Director, an Assessing Officer, an Inspector of Income-tax who has been authorised by the Assessing Officer in relation to the area or part thereof.

Entry of an Income-tax authority to the residential premises of an assessee should enable him to collect further information useful for, or relevant to, the purposes of the Act.

Disclosure of information regarding assessees to certain authorities [Section 138]

(1) The Board or any other authority so authorised by Boad, may furnish or cause to be furnished any information which the income tax authorities have obtained while performing their duties to any officer, authority or body performing any function under any law relating to imposition of tax, duty or cess or in foreign exchange dealings or any other authority so notified.

(2) Such information will be furnished if the Chief Commissioner or the Commissioner is satisfied that it is in public interest to do so.

(3) The Central Government may, by order in Official Gazette, direct that no information or document shall be furnished to any such person except such authorities so notified.

QUESTIONS

1. What are the authorities provided by the income-tax Act for the administraton of tax ? Discuss briefly the powers of Income-tax Officer.
2. Write short notes on:
   (*i*) Central Board of Direct Taxes,
   (*ii*) Commissioner of Income-tax,
   (*iii*) Deputy Commissioner of Income-tax.
3. What are the powers of the Commissioner of Income-tax in regard to search and seizure under Section 132 of the Income-tax Act ? *(B.Com. Punjab, 1976)*

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2 PROCEDURE FOR ASSESSMENT

Introduction—Income-tax returns—Various types of returns—Types of assessments—Self assessment—Pro-visional assessment—Regular assessment—New provisions of regular assessment—Best judgment assessment—Reassess-ment—Rectification of mistake—Notice of demand—Misc. provisions—Questions.

Computation of Total Income is one but major part of the procedure involved in levying tax on an assessee. The process of assessing the income returned and determination of tax payable can be described as assessment. The word 'assessment' has been used in the Income-tax Act meaning differently at different places. On certain occasions it refers to computation of income, sometimes to the determination of tax payable and sometimes to the whole procedure laid down in the Act of imposing liability on the tax payer.

While using the word 'Assessment' in its most comprehensive sense, i.e., including the whole procedure for imposing liability upon the tax-payer, the method for assessment of tax can be divided into three steps:

(*a*) Computation of Tax payable income or taxable income,

(*b*) Computation of tax payable on such taxable income, and

(*c*) Serving of notice of demand in prescribed form.

Computation of total income of an assessee can be done only when he has furnished particulars of his income. The Act makes it the obligation of each and every person to submit particulars of the income relating to a particular accounting period to the Income-tax Officer of his area in prescribed form. This prescribed form is known as 'Return of Income' and its filing is first step towards assessment procedure.

INCOME TAX RETURNS

Voluntary filing of Return [Section 139 (1)]

Section 139 (1) of Income-tax Act demands that every person whose total income or the total income of any other person in respect of which he is assessable during the previous year, exceeds the exempted income, should file a return of his income within the prescribed period voluntarily.

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Due Dates for filing of return [Section 139 (1) (Explanation)]

I. In case of Company assessees	30th November of the Assessment year
II. In case of persons other than companies	
(*a*) In case accounts of the person are to be audited or where report of an accountant is required to be furnished u/s 80HHC, u/s 80HHD or a certificate is to be furnished u/s 80R, RR or RRA or in case of a co-operative society or in case of a working partner of a firm whose accounts are to be audited	31st October
(*b*) In case of non-Company assessees having income under the head "Profits and Gains"	31st August of the Assessment year
(*c*) In any other case	30th June of the Assessment year

In case last date of filing of return is a holiday (office closed) then the next working day shall be deemed as due date for filing of return. [Circular No. 639 Dt. 13.11.92]

With effect from assessment year 1997-98 this new provision is being introduced :-

In case of persons who are not furnishing any return under this section and are residing in notified cities and who at any time during the previous year fulfill any TWO of the following conditions :-

(*a*) Is in occupation of an immovable property exceeding a specified area whether by way of ownership, tenancy or otherwise as may be specified by the CBDT,

(*b*) Is owner or the lessee of a motor vehicle,

(*c*) Is a subscriber to a telephone, or

(*d*) has incurred expenditure for himself or any other person on travel outside India,

He shall be required to file return on or before due date in the prescribed manner.

Interest Chargeable [Sec. 234A]

In case assessee has failed to file the return or has filed the return late, interest @ 2% per month or part thereof is to be charged. Sec. 234 A has made the imposition of interest mandatory.

Interest is to be calculated from the last date of filing of return as allowed u/s 139 (1) to the date of furnishing of the actual return. In case return has not been filed at all interest shall be calculated upto the date of completion of assessment u/s 144.

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Penalty for non filling of return [271F]

In case a person fails to submit his return on or before due date, a penalty of Rs. 500 shall be improved on such person.

Return of loss [Section 139 (3)]

In case a person suffers a loss in any previous year under the head 'business or profession' or 'capital gains' and the person intends to carry it forward, such loss can be carried forward only if such person files a voluntary return of his loss in the prescribed form and verified in the prescribed manner. The loss which the assessee may be able to carry forward shall be of Section 72 (1), 73 (2), 74 (1). With effect from 1.4. 1975, the loss u/s 74 A (3) can also be carried forward along with the loss mentioned in the above given sections. This type of return must be filed within the allowed time u/s 139 (1) and 139 (4). It simply means that the loss of such person cannot be carried forward unless a return of loss voluntarily filed.

Belated Return [Section 139 (4)]

In case an assessee has not furnished a return within the time allowed to him or within the time allowed under a notice served u/s 142 (1), he may furnish the return for any previous year at any time before the expiry of one year from the end of the relevant assessment year or before the completion of the assessment, whichever is earlier.

But in case such situation relates to previous year corresponding to assessment year 1988-89 or earlier assessment years the period allowed shall remain 2 years from the end of relevant assessment year.

Return of Income in case of Trust etc. [Section 139 (4A)]

With effect from assessment year 1989-90 the old provision has been substituted by following 139 (4A). This new provision relates to trusts or institutions. In case total income of such persons or trust exceeds the maximum amount which is not chargeable to tax, such person or trust shall file a return of such income in prescribed form and verified in prescribed manner.

Return of Income in case of Political Parties [Section 139(4B)]

Taxation Laws (Amendment) Act, 1978 has inserted a new sub-section 4B, making it obligatory for chief executive officer of every political party to furnish a return of income of the political party, provided the total income of the political party, as computed under the provisions of this Act without giving effect to this exemption under Section 13A (inserted by the same Act) exceeds the maximum amount which is not chargeable to income-tax.

Revised Return [Section 139(5)]

If any person who has furnished return u/s 139 (1) or in response to a notice u/s 142 (1) discovers any omission or any wrong statement therein he may furnish a revised return at any time before the expiry of one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier.

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In case return relates to previous year relevant to assessment year 1988-89 or any earlier assessment year the time allowed remains 2 years.

Prescribed Form [Section 139 (6)]

The return of income shall be filed in prescribed form and shall be verified in the prescribed manner. An assessee is required to furnish the following particulars:

(*a*) income exempt from tax.

(*b*) assets of the prescribed nature belonging to him and their value.

(*c*) expenditure exceeding the prescribed limits incurred by him under prescribed head and such other outgoings as may be prescribed.

Prescribed Forms of Returns [Rule—12]

(*a*) In case of a company [except these covered in point (c) below] .....Form No.1.

(*b*) In case of a person other than a company.

(*i*) Where the total income includes any income chargeable to tax under the head Profits and Gains of Business or Profession.....Form No. 2.

(*ii*) Where in the case Indian Resident Individual, the total income.....

A. does not exceed Rs. 1,20,000;

B. does not include income taxable under the head "Profits and Gains;" and

C. does not include any brought forward or carry forward loss or allowance except under the head "house property".....Form No. 2A.

(*c*) Where the total income of a person does not include any income taxable under the head 'Profit and Gains, and is not covered under point (*ii*) above,.....Form No.3

(*d*) In case of person (including a company incorporated or not u/s 25 of the Companies Act) who has any income from property held under charitable trust or for religious purposes whose income is exempt u/s 11 of this Act.....Form No. 3A.

Information to Accompany the Return [Section 139 (6A)]

The return filed by any person engaged in business or profession should also provide the following informations. These are:

(*a*) location and style of the principal place and all the branches of the business and profession;

(*b*) name and address of all partners and individuals forming association, etc.;

(*c*) share of each partner, individuals forming an association or a body of individuals;

(*d*) The report of any audit obtained u/s 44 AB or where the report has been furnished prior to the furnishing of return, a copy of such report together with proof of furnishing the report.

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Rectification of defective return [Section 139 (9)]. This new sub-section has been inserted to provide an opportunity to rectify the return already submitted by an assessee.

It provides that if the Assessing Officer finds that the return of income furnished by assessee is defective, he may intimate the defect to the assessee and give him one opportunity to rectify such defect within 15 days from the date of such intimation. Assessing Officer may extend this period at his discretion. In case defect is not rectified in the prescribed time, the notice shall become invalid. In case assessee rectifies the defect after the expiry of aforesaid period but before the assessment is made, the Assessing Officer may condone the delay and thus treat the valid return.

A return of income is regarded as defective unless all the following conditions are fulfilled namely:

(*a*) The annexures, statements and columns in the return of income relating to computation of income chargeable under each head of income, computation of gross total income and total income have been duly filled in.

(*b*) The return is accompanied by a statement showing the computation of the tax payable on the basis of the return.

(*bb*) The return is accompanied by the report of the audit obtained under section 44AB or where the report has been furnished prior to the furnishing of return, a copy of such report together with proof of furnishing of such return.

(*c*) The return is accompanied by proof of the tax, if any, claimed to have been deducted at source and the advance tax and tax on self-assessment, if any, claimed to have been paid.

(*d*) Where regular books of account are maintained by the assessee the return is accompanied by copies of.....

(*i*) manufacturing account, trading account, profit & loss account or, as the case may be, income and expenditure account or any other similar account and balance sheet.

(*ii*) in the case of a proprietary business or profession the personal account of the proprietor; in the case of a firm, association of persons or body of individuals, personal accounts of the partners or members and in the case of a partner or member of a firm, association of persons or body of individuals also his personal account in the firm, association of persons or body of individuals.

(*e*) Where the accounts of the assessee have been audited, the return is accompanied by copies of the audited profit and loss account and balance sheet and the auditor's report and where an audit of Cost accounts of the assessee has been conducted under section 233B of the Companies Act also the report under that section.

(*f*) Where regular books of account are not maintained by the assessee, the return is accompanied by a statement indicating the amounts of turnover or as the case may be, the gross receipts, gross profit, expenses and net

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profit of the business or profession and the basis on which such amounts have been computed and also disclosing the amounts of total sundry creditors, sundry debtors, stock-in-trade and cash balance as at the end of the previous year.

Permanent Account Numbers [139-A]

1. Any person who has not been allotted any permanent account number has to apply for such number to the Assessing Officer for the allotment of permanent account number if he is covered in any of the following categories :-
   (*i*) If the total income of a person exceeds the maximum exempted limit in any of the previous years, or
   (*ii*) If the total income of any other person in respect of whom he is responsible, exceeds the maximum exempted limit in any of the previous years, or
   (*iii*) If the total sales, turnover or gross receipts are or is likely to exceed Rs. 50,000 in any previous year if such person is carrying on business or profession, or
   (*iv*) If any person is required to furnish a return of income under section 139(4A).
2. The Assessing Officer may allot permanent account number to any other person by whom tax is payable under this Act.
3. If any person is not covered under any of the above provisions can also apply for permanent account number.
4. When a person has been allotted a permanent account number and a new series is notified for the area in which he resides, he shall apply for permanent account number in this new series and old permanent account number shall cease to have effect. If permanent account number has already been allotted under new series, he shall not apply again.
5. Such account number shall have to be quoted in :
   (*i*) all his returns, or correspondence with any income-tax authority,
   (*ii*) in all such challans for the payment of any sum due under this Act,
   (*iii*) in all documents pertaining to such transactions as may be prescribed by the C.B.D.T.
   (*iv*) intimate any change in his address or in the name and nature of the business on the basis of which the account number was obtained. This intimation is to be given to the Assessing Officer.
6. Every person who is receiving any document as mentioned at 5 above shall ensure that the permanent account number is mentioned in such document.
7. No person who has already been allotted an account number in new series shall apply or obtain another account number.
8. The C.B.D.T. has been authorised to make rules regarding:-
   (*i*) form and the manner in which application is to be made and the particulars such application shall contain.

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(*ii*) the categories of transactions in which such number has to be mentioned,

(*iii*) the categories of documents in which such number has to be mentioned.

9. The permanent account number in the new series is the number having 10 alphanumeric characters issued in the form of a laminated card.

Signing of Return [Section 140]

According to section 140, the return of income as filed under Section 139, must be signed and verified as follows—

(*a*) in case of individual himself:

(*i*) by the individual himself;

(*ii*) while he is absent from India by the individual himself or by some person duly authorised by him in this behalf.

(*iii*) where he is mentally incapacitated from attending to his affairs, by his guardian or any other person competent to act on his behalf; and

(*iv*) where, for any other reason, it is not possible for the individual to sign the return, by person duly authorised by him in this behalf:

Provided that the person signing on behalf of an individual who is absent from India and for any other reason. [point (ii) and point (iv) above] must hold a valid power of attorney from such individual and which shall be attached to the return.

(*b*) In the case of Hindu Undivided Family, by the Karta and where the Karta is absent from India or is mentally incapacitated from attending to his affairs, by any other adult member of such family.

(*c*) In the case of a local authority, by the principal officer thereof.

(*d*) In case of a company, by the managing director thereof or by any director if there is no managing director or if managing director is not in a position to sign:

"Provided that where the company is not resident in India, the return may be signed and verified by a person who holds a valid power of attorney from such company to do so, which shall be attached to the return."

In case company is being wound up its return shall be signed and verified by the liquidator and in case company has been taken over by the Central or State Government, the return shall be signed and verified by the principal officer of such company.

(*e*) In case of firm, by managing partner thereof, and if managing partner is not available or if there is no managing partner, by any partner not being a minor partner.

(*f*) In the case of any other association by any member of the association or the principal officer thereof.

(*g*) In the case of any other person by that person or by some person competent to act on his behalf.

(*h*) In case of political party, the return is to be signed by the Chief Executive Officer of such party.

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TYPES OF ASSESSMENTS

I. Self Assessment [Section 140A]. Under Section 140A, any tax is payable on the basis of any return being submitted under Section 139 or 142, or 148, the assessee shall deposit the amount of tax, after taking into consideration tax already paid, before the submission of return and the return must be accompanied by proof of payment of such tax.

Tax so paid shall be adjusted towards the tax liability as *ascertained* on regular assessment.

With effect from assessment year 1989-90 the assessee shall be liable to pay such tax together with interest payable under any provision of this Act for any delay in furnishing the return, or any default or delay in payment of advance tax before furnishing the return.

In case the amount falls short of the aggregate of the tax and interest, the amount so paid shall be first adjusted against interest payable and balance shall be adjusted against tax payable.

In case assessee fails to pay the whole or any part of such tax or interest or both in accordance with the provisions of this section, he shall be deemed to be assessee-in-default in respect of the amount not paid by assessee.

II. Enquiry before Assessment [Section 142(1)]. Before finalising the assessment of an assessee, the Assessing Officer may be interested to go through certain books, accounts, documents, statements of the assessee and certain other inquiries, which the Assessing Officer may think desirable before finalising the Assessment. Section 142 empowers the Assessing Officer in this regard. He can issue a notice to the assessee u/s 142 (1), requiring him (assessee) on a date to be specified therein:

(*i*) where such person has, within the time allowed u/s 139 (1) failed, to furnish a return of his income or income of any other person in respect of which he is assessable under this Act, in the prescribed form and verified in prescribed manner and setting forth such other particulars as may be prescribed, or

(*ii*) to produce or cause to be produced, such books, accounts or documents as the Assessing Officer may require, or

(*iii*) to furnish in writing and verified in the prescribed manner information in such form and on such points or matters (including a statement of all assets and liabilities of the assessee whether included in the accounts or not) as the Assessing Officer may require.

(*iv*) The Assessing Officer shall not require production of any books of accounts relating to a period more than three years prior to the previous year. But in the case of documents, there is no such time limit.

U/s 142 (2) for the purpose of obtaining full information in respect of the income or loss of any person, the Assessing Officer may make such inquiry as he considers necessary.

Audit of Accounts in certain cases [142 (2A)]

If, at any stage of the proceeding before him, the Assessing Officer, having regard to the nature and complexity of the accounts of the assessee and in the

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interests of the revenue, is of the opinion that it is necessary to do so, he may, with the previous approval of the Commissioner, direct the assessee to get the accounts audited by an accountant as defined in the *explanation* given below in sub-section(2) of Section 288, nominated by the Chief Commissioner or the Commissioner in this behalf and to furnish a report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed and such other particulars as the Assessing Officer may require.

The above provisions shall have effect notwithstanding that the accounts of the assessee have been audited under any other law for the time being in force or otherwise. [142 (2B)].

Every report under sub-section (2A) shall be furnished by the assessee to the Assessing Officer within such period as may be specified by the Assessing Officer. [142(2C)]

The Assessing Officer may, on an application made in this behalf by the assessee and for any good and sufficient reason extend the said period by such further period or periods as he thinks fit; however, that the aggregate of the period originally fixed and the period or periods so extended shall not, in any case, exceed one hundred and eighty days from the date on which the direction under sub-section (2A) is received by the assessee.

The expenses of and incidental to, any audit under sub-section (2) (including the remuneration of the accountant) shall be determined by the Chief Commissioner or the Commissioner (which determination shall be final) and paid by the assessee. In case of default of such payment, it shall be recoverable from the assessee in the manner provided for the recovery of arrears of tax. [142 (2D)]

Assessee shall, except where the assessment is made u/s 144, be given an opportunity of being heard in respect of any material gathered for the purpose of the Assessment. [142 (3)]

III. Assessment on the basis of return filed. With effect from assessment year 1989-90 new procedure of regular assessment has been prescribed which is as follows:

1. ***When a return has been filed*** [Section 143(1)(a)]

In case assessee has filed any return u/s 139 or in response to notice u/s 142 (1) and—

(*i*) if any tax or interest is found due on the basis of such return after adjustment of any tax deducted at source, any advance tax paid and any amount paid otherwise by way of tax or interest, then, an intimation shall be sent, to the assessee specifying the sum so payable and such intimation shall be deemed to be a notice of demand issued under section 156 and all the provisions of this Act shall apply accordingly; and

(*ii*) if any refund is due on the basis of such return, it shall be granted to the assessee:

2. Adjustments to be made. In computing the tax or interest payable by, or refundable to the assessee, the following adjustments shall be made in the income or loss, declared in the return, namely:

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(*i*) any arithmetical errors in the return, accounts or documents accompanying it shall be rectified;

(*ii*) any loss carried forward, deduction, allowance or relief, which on the basis of the information available in such return, accounts or document, is *prima facie* admissible but which is not claimed in the return, shall be allowed;

(*iii*) any loss carried forward, deduction, allowance or relief claimed in the return, which, on the basis of the information available in such return accounts or documents, is *prima facie* inadmissible, shall be disallowed.

3. Intimation of adjustment even if nothing is due [143 (1) (a) Proviso]

As per amendment made by the Direct Tax Laws (Second Amendment) Act, 1989 in case any adjustment is made by Assessing Officer an intimation to this effect must be sent to assessee even if no tax or interest is found due from him as a result of such adjustment.

4. Adjustment due to an order of Assessing Officer under some other section [143 (1) (b)]

Where as a result of an order made under section 147 or section 154 or section 155 or section 250 or section 254 or section 260 or section 262 or section 263 or section 264, or any order of settlement made under sub-section (4) of section 245 D relating to any earlier assessment year and passed subsequent to the filing of the return referred to in clause (a), there is any variation in the carry forward loss, deduction, allowance or relief claimed in the return, and as result of which,—

(*i*) if any tax or interest is found due, and intimation shall be sent to the assessee specifying the sum so payable, and such intimation shall be deemed to be a notice of demand issued under section 156 and all the provisions of this Act shall apply accordingly, and

(*ii*) if any refund is due, it shall be granted to the assessee.

The same will be applicable in case of orders issued in respect of a firm or Association of persons and as a result if share of partner or member is affected.

An intimation for any tax or interest due under this clause shall not be sent after the expiry of four years from the end of the financial year in which any such order was passed.

Notice to be served if necessary [143(2)]

Where a return has been made under section 139 or u/s 142 (1) the Assessing Officer shall, if he considers it necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not under-paid the tax in any manner serve on the assessee a notice requiring him, on a date to be specified therein, either to attend his office or to produce, or cause to be produced there, any evidence on which the assessee may rely in support of the return.

No notice under this sub-section shall be served on the assessee after the expiry of twelve months from the end of the month in which the return is furnished, whichever is later.

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Assessment on the basis of evidence [143 (3)]

On the day specified in the notice issued under sub-section (2), or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him on the basis of such assessment.

An intimation sent to the assessee under section 143 (1) or 143 (1B) shall be deemed to be an order for the purposes of section 264.

Adjustment of tax on Regular Assessment [Section 143 (4) *Inserted by the Direct Tax Laws (Second Amendment) Act, 1989)*]

In case regular assessment is made u/s 143 (3) or 144—

(*a*) any tax or interest paid by assessee shall be deemed to have been paid towards such regular assessment;

(*b*) in case any excessive amount has been refunded but amount refundable on regular assessment is less, the excess amount of refund shall be deemed to be tax payable by assessee.

Provisions applicable prior to 1-4-88 to remain applicable [143(5) *Inserted by the Direct Tax Laws (Second Amendment) Act, 1989*]

In case of assessments relating to the period prior to the assessment year 1988-89, the provisions as they stood before 1-4-88 shall remain applicable.

Levy of additional Income-tax [143 (1A)]

The Direct Tax Laws (Amendment) Act, 1989 has inserted this new section with effect from 1-4-89 i.e., assessment year 1989-90. This new section provides that in case the total income of a person exceeds the total income declared by him due to adjustments made u/s 143 (1), the Assessing Officer shall add additional income-tax @ 20% of the tax payable on the excess amount of total income (difference between adjusted total income and total income computed by assessee) in the tax payable on adjusted total income.

In case any refund is due, the amount of such refund shall be reduced by an amount equivalent to the additional income-tax so calculated.

In case amount of adjustments is more than computed total income the additional income-tax will be calculated on tax to be calculated on amount of adjustments as total income.

Illustration. From the particulars given below compute the amount of income-tax, additional income-tax and interest payable by the assessee for the assessment year 1997-98 :-

	Rs.
Total income as returned by assessee	1,10,000
Total income as assessed by Assessing Officer	1,31,000
Tax deducted at source	5,000

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Advance tax paid	12,000
Tax deposited at the time of self assessment	2,000
Date of filing of return	2-12-97
Due date of filing of return	31-8-97

Solution

			Rs.
Total income as assessed by Assessing Officer			1,31,000
Tax on this total income		Rs.	
on Rs. 120,000		21,000	
on Balance Rs. 11,000—40%		4,400	
			25,400
Less: Tax deducted at source		5,000	
Advance Tax paid		12,000	
Tax paid on self assessment not to be considered for calculation of interest		Nil	17,000
Net tax for calculation of Interest			8,400

Interest u/s 234A

Delay in filing of return = 4 months
(Sept. 1997 to Dec. 1997)

Interest @ 2% p.m. = $8,400 \times {}^{2}/_{100} \times 4m$ = 672

Additional Income-tax u/s 143(1A)

Income returned by assessee			1,10,000
Tax on this income = 60,000 —		3,000	
	50,000 – 30%	15,000	18,000
Income Assessed by Assessing Officer			1,31,000
Tax on this income 120,000 —		21,000	
	11,000 – 40%	4,400	25,400
Difference of Tax = [25,400 – 18,000] =			7,400
Additional income-tax = 20% of Rs. 7,400 =			1,480

Total Amount Payable	Income-tax		25,400
	Interest		672
	Additional Income-tax		1,480
			27,552
Less: Tax deducted at source		5,000	
Advance Tax		12,000	
Tax on self assessment		2,000	
			19,000
Net Amount Payable			8,552

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Assessment on the basis of revised return after regular assessment has been made [Section 143(1B)]

In case an assessee has furnished a revised return u/s 139(5) after an intimation regarding refund or demand has been sent u/s 143 (1) or 143(1A), the Assessing Officer shall proceed as follow:

(*i*) Intimation already sent shall be suitably amended.

(*ii*) In case any demand notice has been issued and as a result of revised return it has to be further enhanced the revised intimation will be sent and it shall have same effect as rectification u/s 156.

(*iii*) In case any refund has been made and as a result of revised assessment—

(*a*) amount of such refund has been enhanced, the difference of amount will be paid to him.

(*b*) if amount of such refund has been reduced, the difference amount will be treated as tax due and shall be payable by assessee.

In all these cases assessee shall remain liable for additional income-tax.

IV. Best Judgement Assessment

In the process of making assessment of an assessee, the Assessing Officer calls for certain informations through notices from such assessees. To know the correct income or loss of an assessee, such informations may be necessary. In case an assessee fails to comply with such notices, the Act has armed the Assessing Officer with wide powers to deal with such cases. To make a best judgment assessment of assessee's income is the most important tool in the hands of the Assessing Officer. This assessment is also known as 'Ex-parte' assessment.

This type of assessment is made when the assessee does not co-operate with the Assessing Officer, and he, in the absence of sufficient information, proceeds with the finalisation of income or loss of the assessee according to the best of his ability, knowledge, judgement, guess-work etc. The idea of this type of assessment is not to punish the assessee for his non-cooperation, but to make the assessment on the basis of the information, and materials the Assessing Officer has gathered. He can base his judgement on the previous returns, local knowledge and repute of assessee's circumstances and all other matters, informations, which he thinks helpful in arriving at reasonably correct assessment of assessee's income.

An assessment u/s 144 is a quasi-judicial process and any quasi-judicial process requires that before arriving at the decision, the assessee must be given an opportunity of being heard and the assessment is to be based on the material gathered by the Assessing Officer and not merely on the guess work. He should not rely on hearsay evidence and his private opinion should not override the honest estimate which is possible on the basis of available informa-tions. In a case *Hardeodas Jagan Nath vs. Assessing Officer 43 I.T.R. 562* it was clearly held that the best judgement assessment would not be justified unless a valid and proper notice has been duly served on the assessee.

The Privy Council in a case *C.I.T. vs. Laxminarain Badridas 5 ITR* 170, 180 explained the whole process of best judgement assessment in the following words:

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"The Officer is to make an assessment to the best of his judgement against a person who is in default as regards supplying information. He must not act dishonestly or vindictively or capriciously, because he must exercise judgement in the matter. He must make what he honestly believes to be the fair estimate of the proper figure or assessment, and for this purpose he must, their Lordship think, be able to take into consideration local knowledge and repute in regard to the assessee's circumstances and his own knowledge of previous returns and assessments of the assessee, and all other matters which he thinks will assist him in arriving at a fair and proper estimate; and though there must necessarily be guess work in the matter, it must be honest guess-work. In that sense, too, the assessment must be to some extent arbitrary."

The best judgement assessment is of two types:

(*a*) Compulsory best judgement assessment.

(*b*) Discretionary best judgement assessment.

Compulsory Best Judgement Assessment

An assessment made u/s 144 is known as compulsory best judgement assessment. A compulsory best judgement assessment shall be made, if any person—

(*i*) fails to file the return u/s 139 (1) and has not made a return or a revised return u/s 139 (4) and 139 (5); or

(*ii*) fails to comply with all the terms of a notice issued u/s 142 (1); or

(*iii*) fails to comply with the directions issued under Section 142 (2A);

(*iv*) having made a return, fails to comply with all the terms of a notice issued u/s 143 (2).

This section provides that the Assessing Officer shall make the assessment of assessee's total income or loss to the best of his judgement after taking into account all relevant material which he had gathered, *and after giving the assessee an opportunity of being heard.*

It shall not be necessary to provide an opportunity of being heard in a case where a notice u/s 142 (1) has been issued before making such assessment.

Provisions applicable prior to 1-4-88 to remain applicable [Section 144 (2)]

The Direct Tax Laws (Second Amendment) Act, 1989 has inserted this sub-section. According to this the provisions of law as they stood prior to 1-4-88 shall remain applicable to an assessment relating to the assessment year 1988-89 or any prior assessment year.

Issue of Directions by Deputy Commissioner [Section 144A]

In case Deputy Commissioner is of the view that keeping in view the nature of the case or amount of tax involved, it is necessary to issue directions to the Assessing Officer, he may issue such instructions which may enable the Assessing Officer to complete the assessment. Such directions may be issued by the Deputy Commissioner either of his own motion or on request from Assessing Officer.

In case directions are prejudicial to the assessee, an opportunity of being heard must be provided to the assessee.

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Consequences

Along with best judgement assessment, the assessee will also face the following consequences:

(*i*) When the assessee files an application of appeal against the best judgement assessment, he is prevented from bringing on record any new facts before the appellate authorities.

(*ii*) The assessee becomes liable for penalties and prosecutions u/s 271, 276 CC and 276 D.

Remedies

When a best judgement assessment is made against any assessee, he has only two remedies against such assessment. These are:

(i) Filing of an application with the Assessing Officer for the cancellation of the best judgement assessment

Within one month of the service of the notice of demand on the basis of the best judgement assessment u/s 144, the assessee can apply to the Assessing Officer for the cancellation of such assessment. Section 146 empowers the Assessing Officer to cancel the best judgment assessment. But the cancellation can only be there if the assessee applies on the basis of the following grounds. These are:

(*i*) that the assessee was prevented by sufficient cause from making the return required u/s 139, or

(*ii*) that he did not receive the notice issued u/s 142 (1) and 143 (2), or

(*iii*) that he did not have reasonable opportunity to comply or was prevented by sufficient cause from complying with the notice issued u/s 142 (1) and 143 (2).

If the Assessing officer is satisfied with the reasons forwarded by the assessee for non-compliance he must cancel the best judgement assessment and should proceed with the making of regular assessment.

Every application made for cancellation of best judgement assessment shall be disposed of within ninety days from the date of receipt of application by Assessing Officer.

If the Assessing Officer refuses to cancel the best judgement assessment the assessee has been given a right to file an appeal against the best judgement assessment. This right has been granted u/s 216 of the Act. The appeal is presented before the Deputy Commissioner (Appeals) and against his orders, to the Commissioner (Appeals) and Appellate Tribunal. If any question of law arises, the assessee can also knock at the door of High Court and then Supreme Court.

(ii) Filing of an appeal against such assessment with the higher authority

This remedy is not helpful as the assessee cannot produce any new evidence before the Appellate authority as he had failed to produce such evidence before Assessing Officer.

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Discretionary Best Judgement Assessment

Section 145 (2) empowers the Assessing Officer to make a discretionary type of best judgement assessment. This type of assessment may be made under the following two types of cases:

(*i*) Where Assessing Officer is not satisfied about the correctness or the completeness of the accounts of the assessee, or

(*ii*) Where no method of accounting has been regularly employed by the assessee.

Under these circumstances it is up to the discretion of the Assessing Officer whether to make a best judgement assessment or a regular assessment u/s 143 (3). But once this type of assessment is made and tax is determined, the assessee will have no option but to file an appeal with the higher authority against the best judgement assessment. The Assessing Officer shall have no power to refuse to register the firm or cancel its registration if the assessee is a firm.

V. *Income Escaping Assessment or Reassessment*

Re-assessment [Section 147]

If the Assessing Officer, for reasons to be recorded by him in writing, is of the opinion that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of section 148 to 153, assess or re-assess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or re-compute the loss or the depreciation allowance or any other allowance, as the case may be, for the assessment year concerned (hereafter in this section and in section 148 to 153 referred to as the relevant assessment year):

Where an assessment under sub-section (3) of section 143 or this section has been made for the relevant assessment year, no action shall be taken under this section after the expiry of four years from the end of the relevant assessment year, unless any income chargeable to tax has escaped assessment for such assessment year by reason of the failure on the part of the assessee to make a return under section 139 or in response to a notice issued under sub-section (1) of section 142 or section 148 or to disclose fully and truely all material facts necessary for his assessment for that assessment year.

Production before the Assessing Officer of account books or other evidence from which material evidence could with due diligence have been discovered by the Assessing Officer will not necessarily amount to disclosure within the meaning of the foregoing proviso.

For the purposes of this section, the following shall also be deemed to be cases where income chargeable to tax has escaped assessment, namely:

(*a*) where no return of income has been furnished by the assessee although his total income or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeded the maximum amount which is not chargeable to income-tax;

(*b*) where a return of income has been furnished by the assessee but no assessment has been made and it is noticed by the Assessing Officer that the assessee

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has understated the income or has claimed excessive loss, deduction, allowance or relief in the return;

(*c*) where an assessment has been made, but—

(*i*) income chargeable to tax has been under-assessed; or

(*ii*) such income has been assessed at too low a rate; or

(*iii*) such income has been made the subject of excessive relief under this Act; or

(*iv*) excessive loss or depreciation allowance under this Act has been computed.

Issue of Notice [Section 148]

Before making the assessment, re-assessment or re-computation under section 147, the Assessing Officer shall serve on the assessee a notice requiring him to furnish within such period, not being less than thirty days, as may be specified in the notice, a return of his income or the income of any other person in respect of which he is assessable under this Act during the previous year corresponding to the relevant assessment year, in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed; and the provisions of this Act shall, so far as may be, apply accordingly as if such return were a return required to be furnished under section 139.

Time limit for issuing notice [Section 149]

No notice under section 148 shall be issued for the relevant assessment year,

(*a*) in a case where an assessment under sub-section (3) of section 143 or section 147 has been made for such assessment year;

(*i*) if four years have elapsed from the end of the relevant assessment year, unless the case falls under sub-clause (*ii*) or sub-clause (*iii*);

(*ii*) if four years, but not more than seven years, have elapsed from the end of the relevant assessment year unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to rupees fifty thousand or more for that year;

(*iii*) if seven years, but not more than ten years, have elapsed from the end of the relevant assessment year, unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to rupees one lakh or more for that year;

(*b*) in any other case,

(*i*) if four years have elapsed from the end of the relevant assessment year, unless the case falls under sub-clause (*ii*) or sub-clause (*iii*);

(*ii*) if four years, but not more than seven years, have elapsed from the end of the relevant assessment year, unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to rupees twenty-five thousand or more for that year;

(*iii*) if seven years, but not more than ten years, have elapsed from the end of the relevant assessment year, unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to rupees fifty thousand or more for that year.

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In determining income chargeable to tax which has escaped assessment for the purposes of this sub-section, the provisions of *Explanation* 2 of section 147 shall apply as they apply for the purposes of that section.

TIME LIMIT FOR ISSUING NOTICE FOR REOPENING OF ASSESSEMENT [SECTION 149]

FROM THE END OF-RELEVANT-ASSESSMENT YEAR-	*CASES DECIDED BY WAY OF SCRUTINY ASSESSMENT U/S 143 (3) OR 147*	*ANY OTHER CASE*
UPTO 4 YEARS	If the escaped income is less than Rs. 50,000	If the escaped income is less than Rs. 25,000
UPTO 7 YEARS	If the escaped income is between Rs. 50,000 to 100,000	If the escaped income is between Rs. 25,000 to Rs. 50,000
UPTO 10 YEARS	If the escaped income is more than Rs. 100,000	If the escaped income is more than Rs. 50,000

Assessment in pursuance of an order on appeal etc. [Section 150]

Notice u/s 148 may be issued at any time for the purpose of making an assessment or re-assessment or re-computation in consequence of or to give effect to any finding or direction contained in an order passed by any authority by way of appeal, reference or revision or by a court.

No direction can be issued to make an assessment or re-assessment which would have been time-barred in case it had been made at the time when the order challenged in appeal or revision was made.

Sanction for issue of notice [Section 151]

(1) In case where an assessment under sub-section (3) of section 143 or section 147 has been made for the relevant assessment year, no notice shall be issued under section 148 except by an Assessing Officer of the rank of Assistant Commissioner or Deputy Commissioner:

After the expiry of four years from the end of the relevant assessment year, no such notice shall be issued unless the Chief Commissioner or Commissioner is satisfied, on the reasons recorded by the Assessing Officer aforesaid, that it is a fit case for the issue of such notice.

(2) In a case other than a case falling under sub-section (1), no notice shall be issued under section 148 by an Assessing Officer, who is below the rank of Deputy Commissioner, after the expiry of four years from the end of the relevant assessment year, unless the Deputy Commissioner is satisfied, on the reasons recorded by such Assessing Officer, that it is a fit case for the issue of such notice.

Rates of Tax on Re-assessment

Section 152 (1) provides that in assessment, or re-assessment made u/s 147, the tax shall be chargeable at the rate or rates at which it would have been charged had

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the income not escaped assessment. It means the rates of that assessment year shall apply, to which the escaped income actually belongs.

Dropping of Re-Assessment Proceedings

Section 152 (2) lays down certain specific conditions which, if satisfied, will lead to dropping of re-assessment proceedings u/s 147:

(*a*) assessment is reopened u/s 147 (b);

(*b*) assessee did not file any appeal or revision against the original assessment:

(*c*) Assessee is able to show that he has already been assessed on an amount or to a sum not lower than what he would be rightly liable for even if the income alleged to have escaped assessment had been taken into account or the assessment or computation had been properly made.

Time Limit for Completion of Assessment and Reassessment [Section 153]

The Direct Tax Laws (Amendment) Act, 1987 and the Finance Act, 1989 have completely changed the old provisions of law relating to time limit for completion of assessment. These new provisions are as under:

(*a*) No order of assessment shall be made under section 143 or 144 at any time after the expiry of two years from the end of assessment year in which the income was first assessable.

(*b*) In case return or revised return of income relating to the assessment year 1988-89 or any earlier assessment year is filed under section 139 (4) or 139(5) this time limit is only one year from the end of financial year in which such return is filed.

(*c*) In case a notice under section 148 has been served after 31.3.1987, the assessment u/s 147 has to be completed within 2 years from the end of financial year in which notice u/s 148 was served. [153(2)]

(*d*) In case an assessment is cancelled u/s 146, or as a result of an order of fresh assessment is passed under section 250, 254, 263 or 264, the assessment shall be completed within 2 years from the end of the financial year in which the respective orders are issued. [153(2A)]

(*e*) The above limitation is not applicable in following cases. In these cases assessment may be completed at any time but subject to provision of section 153 (2A). These cases are—

(*i*) where a fresh assessment is made u/s 146

(*ii*) where the assessment, reassessment or recomputation is made as a result of order issued u/s 250, 254, 260, 262, 263 or 264, or an order of any court in a proceeding other than by way of appeal or reference under this Act

(*iii*) where assessment of partner is to be reopened as a consequence of an assessment made of a firm u/s 147. [Section 153 (3)]

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Calculation of period of limitation [Section 153]

For the purpose of calculation of period for completion of assessment the following periods are to be excluded—

(*i*) Time taken on opening or reopening of the proceedings or time given to assessee to be re-heard u/s 129;

(*ii*) the period for which assessment proceedings are stayed by Court order;

(*iii*) the time taken to get the account of the assessee audited under section 142 (2A);

(*iv*) The period (not exceeding 60 days) commencing from the date on which the Assessing Officer received the declaration under sub-section (1) of section 158 A and ending with the date on which order under section 158 A (3) is made by him; or

(*v*) In case where an application is rejected by settlement commission, the period commencing from the date on which such application is made and the date on which order of rejection is received by commissioner.

If, as a result of above exclusion, the period of limitation as referred in 153 (1), (2) or (2A) available to Assessing Officer is less than 60 days, such remaining period shall be extended to 60 days.

PROVISIONS RELATING TO RECTIFICATION OF MISTAKE [Section 154]

The Direct Tax Laws (Amendment) Act, 1987 has substituted section 154 (1) with new one. It has come into effect from assessment year 1989-90 and it is as follows:

1. With a view to rectifying any mistake apparent from the record an income-tax authority may—

(*a*) amend any order passed by it under the provisions of this Act;

(*b*) amend any intimation sent by it under section 143(1); or

(*c*) enhance or reduce the amount of refund granted by it.

1A. Where any matter has been considered and decided in any proceeding by way of appeal or revision relating to an order u/s 154 (1), the authority passing such order may amend the order in relation to any matter other than the matter referred which has been so considered and decided.

2. The authority concerned

(*a*) may make the amendment of its own motion; or

(*b*) may make the amendment if any mistake has been brought to his notice by the assessee; or

(*c*) where the assessment was made by Deputy Commissioner (Appeals) or Commissioner (Appeals) and mistake is brought to the notice by the Assessing Officer.

3. In case the rectification order enhances the tax liability or reduces the amount of refund, the assessee must be served with a notice and reasonable opportunity of being heard must be provided.

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4. Order of rectification shall be passed in writing by the Income-tax authority concerned.

5. As a result of rectification if any refund becomes due, the Assessing Officer shall make such refund.

6. In case any tax becomes due as a result of rectification the Assessing Officer shall issue a notice of demand to assessee.

7. No rectification under this section can be made after the expiry of *four years* from the end of the financial year in which such order was passed.

Rectification of Mistakes not on Record [Section 155]

Under the following cases Assessing Officer is empowered to make amendments in the order of assessment:

(1) *Share from firm assessed upto assessment year 1992-93*

In case it is found that due to assessment or reassessment of firm or due to any changes made in the income of firm u/s 154, 250, 254, 260, 262, 263 or 264, or any modification is made in total income of firm on its application u/s 245 D(4) and share of income from such firm has not been added or has been incorrectly added in the income of partner, the Assessing Officer may rectify the order and period of 4 years will be counted from the end of financial year in which the final order was passed in case of firm. [Section 155 (1)]

(2) *Remuneration received by a partner from a firm*

In case of assessment or reassessment of firm or any change in income of firm u/s 154, 250, 254, 260, 262, 263, 264 or any modification in total income of firm is made on its application u/s 245 D (4) and it is found that any remuneration paid to a partner is not deductible u/s 40 (b) of the Act, the Assessing Officer may amend the order of assessment of the partner and period of 4 years shall be counted from the end of financial year in which the final order was passed in case of firm. [Section 155 (1A)]

(3) Above provision is also applicable in case of a member of an association of persons or of a body of individuals. [155 (2)].

(4) Re-computation of total income of an assessee as a result of re-computation of depreciation or a loss. [155 (4)].

(5) Rectification of assessment on withdrawal of Investment Allowance [Section 155 (4A)].

Where assessee has claimed Investment Allowance in an earlier previous year and which is withdrawn later on because of transfer of asset within 8 years or the assessee does not utilise the amount of reserve for the purpose of acquiring new asset within 10 years or reserve is utilised by way of distribution as dividend or creation of asset outside India within 10 years, Investment Allowance originally allowed shall be deemed to have been wrongly allowed and as such the Assessing Officer may

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re-compute the income for that previous year. The re-computation shall be done within 4 years and the period of four years shall be reckoned from:

(*i*) in case of transfer of asset previous year in which asset was transferred;

(*ii*) from the end of ten years of non-utilisation of reserve amount for acquisition of new asset; and

(*iii*) the previous year in which the amount of reserve is misutilised.

(6) On infringement of conditions laid down for grant of development rebate, development allowance. For this purpose the period of four years will be counted from the previous year in which infringement took place. [155(5) and 5A].

(7) Where assessee had claimed deduction of any expenditure on scientific research u/s 35 (2B) and it fails to furnish a certificate of completion of programme within prescribed time (1 year), the deduction claimed in excess of actual expenditure shall be deemed to have been wrongly made and Assessing Officer can make the necessary rectification. [Section 155 (5B)].

(8) In case of company for recomputation of distributable income where an order u/s 104 has been passed. [155 (7)].

(9) Where capital asset was transferred to a company by its subsidiary company or by subsidiary company to its parent company and it is either converted into stock-in-trade by such recipient company or parent company or parent company ceases to hold 100% of share capital of subsidiary company—the Assessing Officer may recompute the income of such company and deemed capital gain (47A) shall be included in the income of such company. Assessing Officer can make such order within 8 years in case of conversion and within 4 years in other. [155 (7B)].

(10) In case of long-term capital gains being invested in *rural development bonds or any other notified security* within six months after the date of transfer under the provisions of Section 54E. [155(10A)].

Notice of Demand [Section 156]

After the assessment order is passed by the Assessing Officer, assessee is informed about this under section 156, and if, any tax, interest, penalty, fine or any other sum is payable in consequence of any order passed under this Act, the Assessing Officer shall serve upon the assessee a notice known as 'Notice of Demand', in the prescribed form specifying the sum so payable. In case assessee does not receive or premises are locked, the notice of demand shall be pasted on the outer wall of the premises and it will be deemed to be the service of notice.

After finishing the assessment work, the Assessing Officer should within reasonable time issue a notice of demand upon the assessee and the assessee should pay the amount specified in the demand notice within 35 days of the serving of the notice at the place and to the person mentioned in the notice.

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The granting of time limit of 35 days can be enhanced or reduced by the Assessing Officer. But the Assessing Officer cannot reduce it without the prior approval of Assistant Commissioner of Income-tax by proving that granting of full days will be detrimental to revenue.

Intimation of Loss [Section 157 (3)]

If there is any amount payable by the assessee as computed under the provisions of this Act, he is served with a notice of demand but in case there is a loss (as computed by the Assessing Officer), the same is also notified by the Assessing Officer to the assessee concerned in writing. The assessee shall be entitled to carry forward and set off of the loss notified by the Assessing Officer.

Intimation of assessment of firm [Section 158]

According to Section 158 whenever a registered firm or an *unregistered firm* is assessed as a registered firm [u/s 183(b)] the Assessing Officer shall notify to the firm by an order in writing the amount of total income of the firm assessed and the apportionment thereof between the several partners. This provision is applicable on such firms for the period prior to assessment year 1993-94.

Special provisions for avoiding repetitive appeals

The Taxation Laws (Amendment) Act, 1984 has inserted following provisions in the Income tax Act, 1961 with effect from assessment year 1985-86. These provision give powers to Assessing Officer and other appellate authorities to dispose of a case in which a question of law identical to a point which is pending with High Court or Supreme Court, is involved. These provision are:

1. *Furnishing of declaration.* [Section 158 A (1)]. Where an assessee claims that any question of law arising in his case for another assessment year is pending before High Court or Supreme Court, he may furnish to the Assessing Officer or the appellate authority, a declaration in prescribed form. Through this declaration he may request that if the Assessing Officer or appellate authority agrees to apply in the relevant case the final decision in the other case, he shall not raise such question of law in this relevant case in appeal before any appellate authority or in reference of High Court or Supreme Court.

2. *Calling for report from Assessing Officer* [Section 158A (2)]. When such declaration (as above) is filed before an appellate authority, such authority shall call for a report from the concerned Assessing Officer about the correctness of such claim. Assessing Officer shall submit such report or can request to the appellate authority to give him an opportunity of being heard.

3. *Disposal of claim* [Section 158 A(3)]. The Assessing Officer or other appellate authority before whom such declaration is filed, may, by order in writing—

(*a*) admit the claim of the assessee if it is satisfied that question of law involved in such case is identical with the point involved in other case; or

(*b*) reject such claim, if not satisfied.

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4. *Issuing of assessment order* [Section 158A (4)]. Where the claim is admitted, the relevant authority will dispose of the case and make the assessment without awaiting for the final decision of the Court.

When such assessment is made assessee shall not have any right to go in appeal to any authority or Court regarding such question of law involved in such case.

5. *Application of final decision.* [Section 158A(5)]. When the decision on question of law in other case becomes final, it shall be applied to the relevant case and Assessing Officer or the appellate authority shall, if necessary, amend the order as issued in sub-section (4) above.

6. *Order u/s 158A (3) to be final* [Section 158A (6)]. The order of Assessing Officer or other appellate authority admitting or rejecting the claim u/s 158A (3) shall be final and cannot be challenged by way of appeal, reference or revision under this Act.

SPECIAL PROCEDURE FOR ASSESSMENT OF SEARCH CASES

With effect from 1.7.95 a new procedure has been provided by inserting these new sections 158 B to 158 BH.

1. When this procedure will be applicable ? [Section 158BA(1)]

These provisions shall be applicable only in those cases where a search is initiated u/s 132 or books of account, other documents or any asset are requisitioned u/s 132A in the case of any person after 30.6.95.

2. The rate at which income will be assessed ? [Section 158BA(2)]

The total undisclosed income will be assessed at flat rate prescribed u/s 113 which is 60%. Total income of the block period shall be subject to this rate irrespective of the fact whether it relates to one or more previous years and whether the assessment of such previous years is pending or not.

3. What is the treatment of income which relates to current previous year ? [Section 158BA(3)]

In case assessee is able to prove to the satisfaction of the Assessing Officer that the undisclosed income includes any income which relates to the previous year which has not ended yet or the last date of filing of return for such previous year has not expired and such income has been properly recorded before the search was made or before any requisition was made, such income shall not be included in the block income for assessment under this section.

4. How to compute undisclosed income ? [Section 158BB(1)]

(*i*) undisclosed income shall be computed for the block period,

(*ii*) it shall be the aggregate of the total income of the previous years falling within such block period,

(*iii*) it shall be computed in accordance with the sections 14 to 80 of the Act,

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(*iv*) it shall be computed on the basis of evidence or documents and such other material or information as the Assessing Officer is able to collect,

(*v*) it shall be reduced by the aggregate of the total income or shall be increased by the aggregate of the losses of such previous years as determined in following cases :-

(*a*) total income or loss as determined if assessment u/s143 or 144 or 147 has been completed,

(*b*) if the person has filed his return of income u/s 139 or 147 and assessment has not been completed, the income disclosed in such return,

(*c*) no adjustment shall be made if due date of filing of return has expired but no return has been filed,

(*d*) in case the previous year has not expired or due date of filing of return has not expired any income which has been duly recorded in the books of account or other documents maintained in the normal course,

(*e*) in case any income is assessed under the orders of the Settlement Commission,

(*f*) where an assessment has already been made earlier u/s 158 BC, income so assessed.

The following points will have to be kept in consideration while making the above adjustments :-

(*i*) the provisions relating to carry forward and set off of losses and unabsorbed depreciation shall not be applicable.

(*ii*) in case of firm the method of allocation of undisclosed income amongst partners shall be same as adopted for allocation of assessed or returned income.

(*iii*) any assessment made u/s 143(1) or 143(1B) shall be deemed as assessment made u/s 143.

4. Treatment of deemed incomes u/s 68, 69, 69A, 69B and 69C [Section 158BB(2)]

In computing the undisclosed income the provisions of section 68, 69, 69A, 69B and 69C shall apply in same manner and the term financial year shall have reference to the relevent previous year falling in the block period and shall include the previous year which ends on the date of search of the requisition.

5. Burden to prove [Section 158BB(3)]

It will be the responsibility of the assessee to satisfy the Assessing Officer that a particular income has already been included in any return of income filed by him before the commencement of search or requisition proceedings.

6. Set off and carry forward of lossess and unabsorbed depreciation [Section 158BB(4)]

Any loss brought forward from earlier years or unabsorbed depreciation cannot be adjusted from undisclosed income but can be adjusted from regular income.

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7. Procedure for block assessment [Section 158BC)]

In case any search has been conducted or requisition has been made u/s 132 or 132A :-

(*a*) The Assessing Officer shall serve a notice on such person asking him to file a return in prescribed form in same manner as under section 142(1)(i). The return has to be submitted within a period of not less than 15 days but not more than 45 days. The return must relate to his total income including the undisclosed income for the block period. No notice is required to be issued u/s 148. No revised return can be filed under this section.

(*b*) The Assessing Officer shall proceed to determine the undisclosed income of the block period and provisions of sections 142(2), 142(3) and 144 shall also be applicable in same manner,

(*c*) After the income of the block period has been determined the Assessing Officer shall pass assessment order and shall determine the tax payable by such person,

(*d*) The assets seized u/s 132 or requisitioned u/s 132A shall be retained to the extent it is necessary and provisions of section 132B shall apply. The term regular assessment or reassessment shall be deemed to refer to block assessment.

8. Undisclosed income of any other person [Section 158BD]

In case Assessing Officer is satisfied that any undisclosed income belongs to any other person, other than the person with respect of whom search has been made, then the books of account, documents or assets relating to such income shall be handed over to the Assessing Officer having jurisdiction on such person.

9. Time limit for completion of block assessment [Section 158BE]

(*i*) The orders under this section shall be passed :-

(*a*) Within one year from the end of month in which last of the authorisation for search u/s 132, or requisition under section 132A was executed and in cases where a search is initiated or books of account or other documents or any assets are requisitioned after 30.6.1995 but before 1.1.1997 ;

(*b*) Within two years if such case occurs on or after 1.1.1997.

(*ii*) The period of limitation under this section for other persons as referred in section 158 BD, shall be :-

(*a*) Within one year from the end of the month in which the notice under this chapter was served on such other person in respect of search initiated or books of accounts or other documents or any assets were requisitioned during 1.7.95 to 31.12.97 ;

(*b*) Within two years if such case occurs on or after 1.1.97.

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10. No penalties or interests to be levied [Section 158BF]

Interest under sectioned 234A, 234B, or 234C and penalties u/s 271(1)(c), or 271A or 271B shall not be levied or imposed upon the assessee in respect of undisclosed income determined under block assessment.

11. Levy of interest and penalty in certain cases [Section 158BFA]

(*i*) In case no return or delayed return is filed by the person after having been served a notice u/s 158 BC(c), such person shall be liable to pay simple interest @ 2% of the tax on undisclosed income for every month or part thereof for the period between :

- (*a*) the day following the expiry of time specified in the notice and upto the date of filing of return of in case of delayed filing of return ;
- (*b*) the day following the expiry of time specified in the notice and upto the date of completion of assessment if no return is filed.

(*ii*) The Assessing officer or the Commissioner (Appeals) in the course of proceedings under these section can impose a penalty of an amount equal to 100% of tax leviable on such undisclosed income as determined u/s 158 BC(c).

The penalty under this section shall not be imposed if :-

- (*a*) such person has furnished a return under section 158 BC(a);
- (*b*) the tax payable on the basis of such return has been paid ; or if the seized assets consist of money and the assessee has offered the money so seized for adjustment against payment of tax;
- (*c*) evidence of tax paid has been furnished alongwith the return; and
- (*d*) no appeal is filed against the assessment of income as shown in return.
- (*e*) Incase there is difference between the returned income and assessed income, the penalty shall be imposed on the tax due on difference of such incomes.

(*iii*) No order of penalty shall be issued :

- (*a*) Unless the assessee has been given a reasonable opportunity of being heard;
- (*b*) The Assistant Commissioner or Assistant Director have taken the prior approval of Deputy Commission or Deputy Director, if amount of penalty exceeds Rs. 20,000;
- (*c*) In case of assessments which are subject matter of appeals with Commissioner (Appeals) u/s 246 or Appellate tribunal u/s 253, after the expiry of financial year in which action for imposition of penaly was initiated or 6 month from the end of the months in which orders on appeal were made by the appropriate authority, whichever period expires later.
- (*d*) In case of revision u/s 263 after the expiry of 6 month from the end of the month in which such revision orders were issued.
- (*e*) In all other cases after the expiry of the financial year in which proceedings for imposition of penalty were initiated or within 6

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months from the end of months in which action for impiring penalty was initiated, whichever expires later.

For the purposes of limitation the time taken in giving an opportunity of being heard; period of immunity granted u/s 245H and the period during which proceeding were stayed due to court orders, shall not be counted. Any authority levying penalty shall inform the Assessing officer in case such authority itself is not Assessing Officer.

12. Prescribed authority for block assessment [Section 158BG]

The orders under block assessment shall be issued by an Assessing Officer not below the rank of Assisstant Commissioner and that too after obtaining the prior approval of the Deputy Commissioner or Deputy Director.

13. Meaning of Block Period

It is the period of previous years relevent to 10 assessment years preceeding the previous year in which search was conducted or requisition was made.

All the other provisions of this Act shall remain applicable in the same manner. [Section 158BH].

QUESTIONS

1. What do you understand by Best Judgement Assessment ? Under what conditions is it made by the Assessing Officer ? On what grounds can a Best Judgement Assessment be cancelled ? *(B.Com. Punjab)*
2. Under what circumstances can an *ex-parte* assessment be made by Assessing Officer? What are the remedies available to the assessee ? *(B.Com. Guru Nanak)*
3. What is Best Judgment Assessment ? What are the circumstances under which it can be made ? State the remedies available to the aggrieved party in such case. *(B.Com. Kurukshetra)*
4. Describe briefly the Income-tax relating to the following:
   (*a*) Income Escaping Assessment.
   (*b*) Rectification of mistake. *(B.Com. Kurukshetra)*
5. Write notes on:
   (*i*) Belated return, (*ii*) Self assessment, (*iii*) Remedies against Best Judgment Assessment, (*iv*) Discretionary Best Judgment Assessment, (*v*) Time-limit for the completion of Assessment.
6. The Income-tax Act has provided the Assessing Officer with vital powers to assess the income of any person. Discuss.
7. What is time limit for filing of return of income under the Income-tax Act ? *(B.Com. Hons., Delhi)*
8. Explain the procedure regarding assessment with special reference to summary procedure i.e., completion of assessment u/s 143 (2). *(B.Com. Punjab)*
9. Explain the provisions relating to "Block Assessment" of undisclosed income ?

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3 COLLECTION OF TAX

Deduction of tax at source—Salaries, interest on securities, dividends, other interest—Casual incomes—Payment to contractors—Payment to Partners—Payment to non-residents—Questions.

The tax on total income is collected in three ways—

(*i*) Deduction of tax at source;

(*ii*) Advance tax; and

(*iii*) Tax on assessment through demand notice *i.e.* direct payment of tax.

DEDUCTION OF TAX AT SOURCE

In certain specified cases of income, tax at source should be deducted by the person responsible for making payment of such income. Income-tax Act provides that such tax must be deducted from the amounts of both residents and non-residents according to the rates prescribed in the Finance Act of that year.

The specified cases of income where tax is deductible at source are normally those cases where the income can be calculated in advance, *i.e.*, the assessee can know his income even before the expiry of that previous year. Generally, in these cases assessee's income, may be more or less, is known. Sections 192 to 206 deal with the deduction of tax at source.

The specified cases where tax is deducted at source are: salaries, interest on securities, interest other than interest on securities, dividends, winning from lotteries and crossword puzzles, payment to contractors, insurance commission, winning from horse races and also on other sums chargeable under the Act, which are paid to non-residents.

The provisions of the Act, in each case, are given below:

Salaries [Sec. 192]

U/s 192 (1) any person responsible for paying any income chargeable under the head 'Salaries' (Sec. 15) shall at the time of payment, deduct income-tax on the amount payable at the average rate of income-tax computed on the basis of rates in force for the financial year in which the payment is made, on the estimated income of the assessee under this head for that financial year. It means deduction should be made where an amount is paid and it should be calculated at the rate prescribed for the year in which the payment to the employees is made. [*C.I.T. v. Srinivasan 83 I.T.R. 346 (S.C.)*]

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The Finance Act, 1987 has inserted the following provisions in case of salaried employees:

(*i*) *Employment under more than one employer during relevant previous year.* The assessee must furnish details of his salary received from previous employer to the present employer for deduction of tax at source [u/s 192 (2)].

(*ii*) *Relief u/s 89 (1).* In case any arrears are paid to an employee working in any Government organisation or company, co-operative society, local authority, University, institution, association or body, and he is entitled to relief u/s 89 (1), he may apply to his employer and employer can allow relief u/s 89 (1) [u/s 192 (2A)].

(*iii*) *Income from any other head.* A salaried employee can furnish details of his other incomes to his employer and employer can deduct tax at source for such incomes also. *But assessee has no right to claim the set off of any loss from any other head. [Section 192 (2B)].*

Section 192 (3) provides that the person making the payment of salary may, at the time of making any deduction at source, increase or reduce that amount to be deducted under this section for the purpose of adjusting any excess or deficiency arising out of any previous deduction or failure during the financial year.

In case where the accumulated balance in an unrecognised provident fund and employer's contributions in the superannuation fund and interest on such contributions is not exempt from tax, whenever any payment due to an employee out of these funds is made, the person responsible for making such payment shall deduct tax while making such payment. [Section 192 (4) and (5)].

Section 192 (6) says that for the purposes of deduction of tax on salary in foreign currency, the value in rupees of such salary shall be calculated at the prescribed rate of exchange.

The employer must deduct tax at source from the salary of his employees where it is taxable and so the employer has no right to negotiate with any employee an arrangement whereby the employee has undertaken to discharge his tax liability himself.

Tax at source is deductible from the salaries of only those employees whose income for a previous year exceeds the minimum taxable limit. The person responsible for making such deduction must deposit the tax in the government treasury within the prescribed period and according to the prescribed manner.

Rates of Tax to be deducted at source

The schedule containing rates of tax to be deducted at source is given in Part III, Chapter 1 of this book.

Interest on Securities [Section 193]

Section 193 deals with deduction of tax at source from income chargeable by way of "Interest on Securities". The person responsible for paying interest on securities is liable to deduct income-tax at the time of paying the interest. Here again, tax shall be deducted according to the rates specified by the Finance Act of the year.

Tax at source shall not be deducted in the case of following securities:

1. 4.25% National Defence Bonds, 1972, where the Bonds are held by a resident individual;

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2. 41/2% National Defence Loan, 1968 or 43/4% National Defence Loan 1972;

3. National Development Bonds;

4. Seven-year National Saving Certificates, Fourth Issue;

5. Debentures issued by any co-operative society or any other approved institution or authority or public sector company, so notified;

6. 61/2 per cent Gold Bonds, 1977, or 7 per cent Gold Bonds, 1980, where the bonds are held by a resident individual. However, the total nominal value of 61/2 per cent Gold Bonds, 1977, or the 7 per cent Gold Bonds, 1980 should not exceed Rs. 10,000; and

7. Any other security of the Central or State Government where the security is held by a resident individual and the holder has not been previously assessed to income-tax and his total income of the previous year is not likely to exceed the exempted amount of Rs. 40,000 and the total nominal value of the securities does not exceed Rs. 2,500.

8. Tax shall not be deducted on any interest payable on such securities of Central Government or State Government to such class of persons and subject to certain conditions, as the Central Government may, by notifications in the Official Gazette, specify in this behalf. (*Being deleted with effect from 1-6-97*)

With effect from 1-6-97 no tax will be deducted at source on any interest payable on any security of Central Govt. or a State Government.

9. Interest on debentures issued by a public sector company. In case of any other company, tax on interest on debentures shall not be deducted provided—

(*i*) the interest is paid by a public limited company;

(*ii*) the debentures are listed on a recognised stock exchange;

(*iii*) the interest is paid to an individual;

(*iv*) it is paid by an account payee cheque; and

(*v*) the amount of such interest or aggregate of the amounts of such interest paid or likely to be paid does not exceed Rs. 2,500 in a previous year.

Dividends [Section 194]

Section 194 deals with deduction of tax at source from dividends paid by an Indian company or a company which has made the prescribed arrangements for the declaration and payment of dividends within India to a shareholder who is resident in India.

Rule 30A provides for giving credit in respect of tax deducted at source to a person other than the registered shareholder in certain circumstances.

It is further provided that in case an individual shareholder proves through a certificate provided by the Assessing Officer that his income including dividend income is less than minimum liable to income-tax, tax at source shall not be deducted from the dividend paid to such individual shareholder.

No deduction of Tax at Source. With effect from 1-4-84 Section 194 has been amended and as a result no tax will be deducted at source by the authority paying dividend if following conditions are fulfilled:

(*i*) Dividend is paid to an individual;

(*ii*) Shares are listed on a recognised stock exchange in India;

(*iii*) Shares are issued by a company in which public are substantially interested;

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(*iv*) The aggregate of dividend payable on such shares in the financial year does not exceed Rs. 2,500;

(*v*) The dividend or interest must be paid in account payee cheque.

With effect from 1-6-97 there will be no TDS in respect of any dividend declared, distributed or paid.

Interest (Other than Interest on Securities)

Section 194-A enjoins deduction of tax at source from interest other than that which is not chargeable by way of 'Interest on Securities'.

Under Section 194-A (1) any person, not being an individual or a H.U.F. who is responsible for paying to a resident any income by way of interest other than income chargeable as 'Interest on Securities' shall at the time of credit of such income to the account of payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is there, deduct income-tax thereon at rates in force in that assessment year.

Tax at source shall not be deducted from the amount of interest payable to a person (not being a company or a registered firm) in case such person furnishes—

(*a*) affidavit, or (*b*) a statement in writing declaring that his estimated total income assessable for the assessment year next following financial year in which the income is credited or paid will be less than the minimum liable to income-tax.

Tax at source is also not deductible when such interest is payable to

(*i*) any Banking company or any cooperative society engaged in carrying on the business of banking (including co-operative land mortgage Bank) except in case of term deposits; [Section 193 (3)]

(*ii*) any financial corporation set up under Central, State or Provincial Act;

(*iii*) Life Insurance Corporation of India;

(*iv*) Unit Trust of India [Except on certain interests covered u/s 194K]

(*v*) any company or cooperative society engaged in business of Insurance;

(*vi*) any other institution, association or body, so notified by central Govt.;

(*vii*) any income paid by a cooperative society to a member or to any other cooperative society except interest paid by a cooperative society engaged in banking business covered u/s 194A (Proviso);

(*viii*) any income paid in respect of a deposit so notified by central Govt.;

(*ix*) any income credited or paid in respect of deposits (other than time deposits) with a bank;

(*x*) any income credited or paid in respect of deposits with primary agricultural society or a primary credit society or a cooperative land mortgage Bank or a cooperative land development bank or deposits with a cooperative society (other than time deposits engaged in carrying on the business of banking).

No deduction of tax at source is made where the aggregate of the amounts of such incomes credited or likely to be credited or paid during the financial year does not exceed Rs. 2,500. This limit has been raised to Rs. 10,000 for interest on time deposits with banks, coop-society engaged in business of banking or a public company accepting deposits for housing development.

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In case of interest on bank deposits [Section 194A Proviso]

If any interest is paid or credited to the account of a person by a banking company to which the Banking Regulation Act 1956 is applicable including any bank or banking institution or a co-operative society engaged in banking business and amount of interest is more than Rs. 10,000 tax shall be deducted at source at prescribed rates. The amount of interest shall be the income paid or credited by a branch of banking company or co-operative society. This provision has come into effect on 1.7.1995. This provision is applicable only on time deposits made on or after 1.7.1995.

Winnings from Lottery or Crossword Puzzle [Sec. 194B]

Section 194B says that income-tax will have to be deducted at source from any income by way of winning from any lottery or crossword puzzle in case the amount exceeds Rs. 5,000.

In case winnings are wholly in kind, or partly in cash and partly in kind, and amount of cash winnings is not sufficient to meet the TDS liability, the person responsible for making such payment before releasing the winnings must ensure that full tax has been paid in respect of winnings. This provision is being introduced from 1-6-1997.

Winning from Horse Races [Sec. 194BB]

Any person who is responsible for paying to any person any income by way of winning from any horse race an amount exceeding Rs. 2,500 shall, at the time of payment deduct tax at the rate prescribed for such year.

Payment to Contractors [Sec. 194C]

Section 194C enacts that any person responsible for paying any sum to a resident contractor for carrying out the work (including supply of labour for carrying out the work) is required to deduct 2% of the amount payable or credited to the account of the contractor. In case payment is for advertisements rate of tax is 1%.

Section 194C is applicable in case of contract between contractor and

(*a*) The Central Govt; or State Govt; or
(*b*) any local authority; or
(*c*) any statutory corporation; or
(*d*) any company; or
(*e*) any co-operative society; or
(*f*) any authority engaged in providing the housing accommodation or for planning, development or improvement of cities, town, or villages; or
(*g*) any society registered under Societies Act; or
(*h*) any trust; or
(*i*) any university or any institution declared as University by University Grants Commission, or
(*j*) any firm.

Section 194C (2) deals with sub-contractors. Any contractor (not being an individual or a Hindu undivided family) who is responsible for paying any sum to any

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resident sub-contractor in pursuance of a contract with the sub-contractor for carrying out or for the supply of labour for carrying out the whole or any part of the work undertaken by the contractor, is required to deduct an amount equal to *one* per cent of the amount which is paid or credited to the account of the sub-contractor.

A deduction under the provisions of Section 194 C (3) need not be made where the consideration for the contract is Rs. 10,000 or less.

Under Section 194C (4), where the Assessing Officer is satisfied that total income of the contractor or the sub-contractor justifies deduction of income-tax at any lower rate or no deduction of income tax at all, the Assessing Officer is empowered to give a certificate that tax may be deducted at a lower rate or may not be deducted at all as the case may be. Such a certificate holds good till it is cancelled by the Assessing Officer.

It may be noted that the provisions of Section 194C are wide enough to cover not only written contracts but all those which are orally entered into.

It should also be noted that the percentage of deduction prescribed is with reference to the amount of payment itself and not to the element of income or profit which is part of the payment.

Therefore, the person responsible for paying is not required to estimate the income or profit which is embedded in the payment to contractor or sub-contractor.

The term *Contractor* shall also include a contractor who is carrying out anywork (including supply of labour for carrying out any work) under a contract between the contractor and the Government of a foreign State or a foreign enterprise or an association or body established outside India.

The expression 'Work' shall also include :-

(*a*) Advertising ;

(*b*) Broadcasting and telecasting including production of programmes for such broadcasting and telecasting,

(*c*) Carriage of goods and passengers by any mode of transport other than by railways;

(*d*) Catering.

Insurance Commission [Sec. 194-D]

The Finance Act, 1973, introduced Section 194-D whereby tax at source will be deducted by any person responsible for paying to a resident, any income by way of remuneration or reward, whether by way of commission or otherwise or soliciting or procuring insurance business. It must exceed Rs. 5,000.

Payments to Non-Resident sportsmen or sports associations [Section 194E]

With effect from 1st November 1989, where any income as referred u/s 115 BBA is payable to a non-resident sportsman (including an athlete) who is not resident of India or a non-resident sports association or institution, the person making such payment or crediting it to the account of payee shall deduct tax @ 10%.

Payment is respect of deposits under National Savings Scheme [Section 194 EE]

The person responsible for making payment of any amount to any person, who has deposited any amount in National Saving scheme and has claimed deduction u/s 80 CCA, shall deduct income-tax at the rate of 20% provided such payment or aggregate

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amount of payments made during the financial year is Rs. 2,500 or more. This provision shall not be applicable in case of payment of said amount to the heirs of assessee.

Repayment of Units of Mutual Fund covered u/s 80 CCB [194 F]

At the time of repayment of Units of UTI or Mutual Funds on which a deduction u/s 80 CCB was claimed, a tax @ 20% shall be deducted at source.

Commission etc. on sale of lottery tickets [Sec. 194 G]

Any person who is responsible for paying any income by way of commission, remuneration or Prize (by whatever name called) to a person who has been stocking, distributing, purchasing or selling lottery tickets, shall deduct tax @ 10% while making payment of such income in cash or in cheque or bank draft or by any other mode. No tax shall be deducted at source if such income does not exceed 1,000 at any time. The tax will be deducted at source even if income is credited to the account of the assessee or it is credited to the suspense account. This provision came into effect from 1-10-91.

The Finance Act 1992 has added the following two sub-sections to this section which are as follows:

(*i*) In case an assessee files an application to Assessing Officer that tax may be deducted at lower rate, the Assessing Officer may issue a certificate allowing deduction of tax at source at lower rate.

(*ii*) Such a certificate shall remain valid till it is cancelled by the Assessing Officer.

Commission Brokerage etc. [Section 194 H]

This provision was inserted for the period 1.10.91 to 1.6.92 only. Afterwards it has been discontinued by the Finance Act 1992.

Income from Rent [Section 194 I] *(with effect from 1.6.94)*

In case any amount of rent is paid by a person other than individual or H.U.F. the person responsible for making payment or crediting the amount to the account of payee shall deduct income-tax :-

(*a*) 15% if the payee is individual or H.U.F; and

(*b*) 20% in all other cases.

This provision will not be applicable if the total amount of rent credited or likely to be credited during the previous year does not exceed Rs. 1,20,000. The rent means any payment under any lease, sub-lease, tenancy or other arrangement for the use of land, building, factory building, with or without furniture or fittings, whether such building is owned or not.

Fee for professional or technical services [Section 194J]

1. This provision is applicable on all those persons except individuals and Hindu undivided families, who make any payment by way of
   (*i*) fees for professional services, or
   (*ii*) fees for technical services.

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2. It provides for deduction of tax at source at the rate of 5% at the time such payment is made or credited to the account of a person. Payment may be made in cash, cheque or draft.
3. No. tax shall be deducted at source in following cases :-
   (*i*) any amount credited or paid before 1.7.1995.
   (*ii*) any amount credited or paid if such amount does not exceed Rs. 20,000.
4. If Assessing Officer is satisfied that the total income of a person justifies deduction of tax at lower rate, he will issue a certificate to this effect on an application made by such person. The person making payment shall continue to deduct tax at such lower rate till such certificate is not cancelled by the Assessing Officer.
5. The term professional services means services rendered by a person in the course of carrying on legal, medical, engineering, architectural profession or the profession of accountancy or technical consultancy or interior decoration or advertising or such other profession as is notified by the Board. The term technical services shall have the same meaning as is assigned to it in explanation 2 to clause (vii) of sub section (1) of section 9.

Income in respect of units [Section 194K]

1. This provision is applicable on all Mutual Funds set-up u/s 10(23D) and Unit Trust of India.

2. Any person who is making payment or is crediting any amount on behalf of such Mutual Fund or Unit Trust of India shall deduct tax at the rate of :-

(*i*) 20% if the payee is a company, and
(*ii*) 15% in all other cases.

3. No tax will be deducted at source.

(*i*) If aggregate of the amounts paid or credited or likely to be credited or paid during the financial year does not exceed Rs. 10,000. This amount shall be computed with reference to the income paid or credited in respect of a branch office of the Mutual Fund or Unit Trust of India and under a particular scheme under which the units have been issued.
(*ii*) If income is credited or paid before 1.7.95.
(*iii*) If income is credited or paid in respect of units issued under any scheme of Mutual Fund or U.T.I. which is so notified by the Central Government.
(*iv*) If income is credited or paid in respect of units where such income is exempted u/s 10(11), 10(22), 10(22A), 10(23), 10(23AA) or 10(23C).

Any other sums paid to Non-residents [Sec. 195]

It provides that any person responsible for paying to a non-resident not being a company or to a foreign company, any interest, not being 'Interest on Securities' or any other sum except salaries, chargeable to tax shall at the time of payment (unless he himself is liable to pay any income-tax thereon as an agent) deduct income-tax at the prescribed rates for that year.

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No tax shall be deducted at source in case the assessee furnishes a prescribed certificate granted by the Assessing Officer in this respect.

Such certificate is issued and remains in force for a specified period unless it is cancelled by the Assessing Officer before the expiry of such period.

The Board may make rules for the grant of certificate by the Assessing Officer and notify the circumstances under which the assessee can apply for the grant of such a certificate.

In case interest is payable by the Government or a public sector bank [as defined u/s 10(23D)] or a public financial institution, deduction of tax shall be made only at the time of payment thereof in cash or by any other mode.

No TDS on any dividend declared, distributed or paid by Indian Company from 1-7-1997.

Grossing up of Interest [Section 195A]

In case interest is paid net of tax (i.e. tax-free interest) and tax is borne by the issuing authority, such net interest has to be grossed up by multiplying the net interest by 100/(100-rate of tax).

Interest or dividend or other sums payable to Government, Reserve Bank or Certain Corporations [Section 196]

No tax shall be deducted at source by any person on interest or dividend payable to—

(*i*) the Government; or

(*ii*) the Reserve Bank of India; or

(*iii*) a corporation established by or under Central Act which is, under any law for the time being in force, exempt from income tax; or

(*iv*) a Mutual Fund specified under section 10(23D).

Where such sum is payable to it by way of interest or dividend in respect of any securities or shares owned by it, in which it has full beneficial interest or any other income accruing or arising to it.

No deduction of tax at source on sum payable to unit holders of Mutual Fund [Section 196A]

No tax shall be deducted at source from any sums payable to unit holders of a Mutual Fund, or unit holders of U.T.I. to persons other than foreign companies.

In case any income is paid to foreign company on Units of U.T.I. or Mutual Funds, the tax at the rate of *20%* shall be deducted at source [196 A(2)]

In case income is payable, in respect of units issued under any scheme of the Unit Trust of India, to any institution or fund where such income is not liable to inclusion in its total income under section 11, 12, 10(22), 10(22A), 10(23), 10(23AA) or 10(23C) of the Act, no tax shall be deducted at source.

Income from Units of Offshore Fund [Section 196B]

In case any income is payable in respect of Units of Offshore Fund (Section 115AB), tax at the rate of 10% shall be deducted at source at the time of making the

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payment or crediting the amount to the account of payee. This provision has come into effect from 1-10-91.

Income from Foreign Currency Bonds or Shares of Indian company [Section 196C]

In case any income by way of interest or dividend is paid or is payable in respect of Bonds or shares of Indian companies as referred in section 115 AC, income-tax @ 10% shall be deducted at source.

This amendment has been inserted by the Finance Act 1992 and is effective from 1-6-1992.

No TDS on any dividend declared, distributed or paid by Indian Company from 1-7-1996.

Deduction of Tax at Lower Rates [Section 197]

If the Assessing Officer is satisfied that the total income of the recipient justifies the deduction of income-tax at any lower rates or no deduction of income-tax, as the case may be, the Assessing Officer shall, on an application by assessee, give to him such certificate as may be appropriate. This provision is also applicable when a company pays dividend out of tax holiday profits.

No deduction of tax at source on furnishing declaration [Section 197A]

1. No deduction of income-tax will be made from interest on securities, dividends or interest, payable to a resident individual, if he furnishes to the person responsible for paying such interest or income, a declaration in writing in duplicate in the prescribed form and verified in the prescribed manner to the effect that his estimated total income of the previous year in which such income is to be included in computing his total income, will be less than the minimum liable to tax.
2. No deduction of tax shall be made u/s 194 A or 194 K in case interest is paid to a person (not being company or a firm) if such person furnishes a declaration in writing in duplicate to the effect that the tax on his estimated total income of the previous year in which such income is to be included shall be NIL.
3. The authority, to whom such declaration is furnished must forward one copy of such declaration to the concerned Chief Commissioner or Commissioner of Income-tax on or before the 7th day of the month following the month in which such declaration is furnished.

Tax deducted is Income Received [Section 198]

All sums deducted u/s 192, 193, 194, 194A, 194B, 194BB, 194C, 194D, 194E, 194EE, 194F, 194G, 194H, 194I, 194J, 194K and 195, 196A, 196B, 196C shall for the purpose of computing the income of an assessee, be deemed to be income received.

Credit for Tax Deducted [Sec. 199]

Any deduction of tax made in accordance with provisions of Sections 192 to 195 is deemed to have been paid on behalf of the assessee or the person from whom income-tax was deducted and he is given credit for it in his regular assessment.

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Duty of Person Deducting Tax [Section 200]

Any person deducting any tax (at source) shall pay within the prescribed time, he sum so deducted to the credit of the Central Government or as the Board directs.

Consequences on Failure to Deduct or Pay [Section 201]

As it is mentioned earlier, it is the duty of the person paying income to deduct tax at source, but in case he fails to deduct such a tax or after deducting fails to deposit the same as per rules, such person would be deemed to be an assessee in default in respect of the tax and would be personally liable to pay tax as well as penalty which may be imposed.

Deduction only one Mode of Recovery [Section 202]

The power to recover tax deduction u/s 192 to 195 shall be without prejudice to any other mode of recovery.

Certificate for Tax Deducted [Section 203]

It provides that every person deducting tax u/s 192 to 195 shall, at the time of credit or payment of the sum, or, as the case may be, at the time of issue of a cheque or warrant for payment of any dividend to a shareholder, furnish to the person to whose account such credit is given or to whom such payment is made or the cheque or warrant is issued, a certificate to the effect that tax has been deducted and specifying the amount so deducted, the rate at which the tax has been deducted and such other particulars as may be prescribed.

Rule 31 of Income-tax Rules, 1962, prescribes the form of certificate which the person deducting tax will furnish.

Tax deduction account number [Section 203A]

(1) Every person who is responsible for deducting tax at source and who has not been allotted such an account number shall apply to the Assessing Officer within prescribed time for the allotment of Tax-deduction account number.

(2) Such account number shall be quoted on following document:

(*i*) all the challans for the payment of tax.

(*ii*) all tax deduction at source certificates.

(*iii*) all returns to be submitted u/s 206, 206A and 206B.

(*iv*) any other document so prescribed.

Persons responsible for deducting tax at source [Section 204]

(*i*) In case of salaries payable by a person other than Government, the employer himself and if the employer is company, the company itself including the principal officer thereof ;

(*ii*) In case of interest on securities payable by a person other than State of Central Govt., the local authority, corporation or company including the principal officer thereof ;

(*iii*) In case of any other sum paid or credited under the provisions of this Act, the payer himself or if the payer is a company, the company itself including the principal officer thereof.

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Bar against Direct Demand on Assessee [Sec. 205]

Where tax is deductible u/s 192 to 195, the assessee shall not be required to pay tax himself to the extent to which tax has been deducted from that income.

Persons Deducting Tax to Furnish prescribed Returns [Sec. 206]

Every person responsible for deducting tax at source shall within the prescribed time after the end of each financial year, prepare and deliver or cause to be delivered, to the prescribed income-tax authority, such returns in such form and verified in such manner and setting forth such particulars as may be prescribed.

Persons paying interest to resident without deduction of tax, to furnish prescribed return [Sec. 206A]

Any person responsible for paying interest other than interest on securities shall prepare upto 30th April each year and deliver or cause to be delivered to the Assessing Officer in the prescribed form and verified in the prescribed manner a return in writing showing—

(*a*) the name and address of every person who has furnished to him an affidavit or a statement declaring that estimated total income will be less than the minimum liable to income-tax.

(*b*) the amount of the income credited or paid during the financial year to each such person and the time or times at which the same was credited or paid.

(*c*) such other particulars as may be prescribed.

Persons paying dividend to certain residents without deduction of tax to furnish prescribed return [Section 206B]

Any person responsible for paying any dividend referred to in Section 194 shall prepare and within thirty days after 31st March in each year, deliver or cause to be delivered to the Assessing Officer a return in prescribed form in writing showing—

(*a*) the name and address of every person who has furnished to him a statement under the first provision of Section 194;

(*b*) the amount of dividend paid or distributed during the financial year to each such person; and

(*c*) such other particulars as may be prescribed.

Profits and gains from the business of trading in alcoholic liquor, forest produce, scrap etc. [Section 206C]

Every person, being a seller shall, at the time of debiting of the amount payable by the buyer referred to in that section to the account of the buyer or at the time of receipt of such amount from the paid buyer in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier, collect from the buyer of any goods of the nature specified in column (2) of the Table below, a sum equal to the percentage, specified in the corresponding entry in column (3) of the said Table, of such amount as income-tax.

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TABLE

Sl. No.	*Nature of goods*	*Percentage*
1	*2*	*3*
(*i*)	Alcoholic liquor for human consumption (other than Indian-made foreign liquor)	Fifteen per cent
(*ii*)	Timber obtained under a forest lease	Fifteen per cent.
(*iii*)	Timber obtained by any other mode	Five per cent.
(*iv*)	Any other forest product not being Timber as tender leaves	Fifteen per cent.

Provided that where the Assessing Officer, on an application made by the buyer, gives a certificate in the prescribed from that to the best of his belief any of the goods referred to in the aforesaid Table are to be utilised for the purposes of manufacturing, processing or producing articles or things and not for trading purposes, the provisions of this sub-section shall not apply so long as the certificate is in force.

The power to recover tax by collection under sub-section (1) shall be without prejudice to any other mode of recovery.

For the above purposes—

the **Buyer** means a person who purchases by way of auction, tender or any other mode, the goods as given above but does not include:

(*a*) a public sector company ;

(*b*) a buyer in the further sale of goods obtained in pursuance of such sale ; or

(*c*) a buyer buying such goods in auction but the price of such goods is fixed by State Govt.

The **Seller** means the Central Govt.; or State Govt.; or a local authority or a statutory corporation or any authority set up under a Central or State Act or any company, firm or Cooperative Society.

Tax Deducted to be Deposited [206C(3)]

Any person collecting any amount under sub-section (1) shall pay within seven days the amount so collected to the credit of the Central Government or as the Board directs.

Any amount collected in accordance with the provisions of this section and paid under sub-section (3) shall be deemed as payment of tax on behalf of the person from whom the amount has been collected and credit shall be given to him for the amount so collected on the assessment under this Act for the assessment year for which such income is assessable.

Certificate of Tax deducted at source [206C(5)]

Every person collecting tax in accordance with the provisions of this section shall within ten days from the date of debit or receipt of the amount, furnish to the buyer to whose account such amount is debited or from whom such payment is received, a certificate to the effect that tax has been collected and specifying the sum so collected,

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the rate at which the tax has been collected and such other particulars as may be prescribed.

Tax Payment on Default [206C(6)]

Any person responsible for collecting the tax who fails to collect the tax in accordance with the provisions of this section, shall notwithstanding such failure, be liable to pay the tax to the credit of the Central Government in accordance with the provisions of sub-section (3).

Without prejudice to the provisions of sub-section (6), if the seller does not collect the tax or after collecting the tax fails to pay it as required under this section, he shall be liable to pay simple interest at the rate of two per cent per month or part thereof on the amount of such tax from the date on which such tax was collectable to the date on which the tax was actually paid.

Where the tax has not been paid as aforesaid, after it is collected, the amount of the tax together with the amount of simple interest thereon referred to in sub-section (7) shall be a charge upon all the assets of the seller.

ADVANCE PAYMENT OF TAX OR PAY AS YOU EARN

Tax shall be payable in advance during any financial year, in accordance with the provisions of Sections 208 to 219 (both inclusive) in respect of the total income of the assessee which would be chargeable to tax for the assessment year immediately following the financial year, such income being hereafter in this chapter referred to as current income [Section 207].

When the Liability to Pay Advance Tax arises ? [Sec. 208]

Advance tax shall be payable during a financial year in every case where the amount of such tax payable by the assessee during that year, as computed in accordance with the provisions of this act, is Rs. 5,000 or more (with effect from 1.10.1996).

Computation of Advance Tax [Section 209]

(i) Calculation of advance tax payable u/s 210 (1), or (2) or (5) or (6)

Assessee shall first estimate his income and tax shall be calculated on such income at current rates.

(ii) Calculation of advance tax payable u/s 210 (3)

Assessing Officer, while making an order u/s 210 (3) asking an assessee to pay advance tax, shall take into consideration the total income of the latest previous year on which regular assessment has been made or the total income returned by assessee in his latest return whichever is higher, as current income and on which tax shall be calculated at rates applicable in that financial year.

(iii) Calculation of advance tax payable u/s 210 (4)

In case the Assessing Officer is making an amended order, the total income declared in the return furnished by the assessee for the latest previous year or as the case may be the total income in respect of which a regular assessment has been made, shall be deemed as current income on which tax shall be calculated at the rates in force in that financial year.

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Out of the tax so calculated any amount of tax deducted at source shall be deducted and balance shall be the amount of advance tax payable under this section.

(iv) Assessee having agricultural income [Section 209(2)]

For calculation of advance tax, the agricultural income shall be integrated with current income if the Finance Act of such financial year so provides.

(v) Calculation of advance tax payable by special HUF [Section 209(3)]

The advance tax in case of an HUF (having at least one member whose individual income exceeds Rs. 30,000) shall be calculated on its current income at rates specified for such H.U.F. in the Finance Act of relevant financial year. [209 A (1 to 5)]

Payment of Advance Tax [Section 210]

(i) Voluntary payment of advance tax [Section 210(1)]

It is the duty of every assessee whether or not assessed previously to tax, to deposit the amount of advance on or before each of the due dates specified in section 211, in equal instalments.

(ii) Increase or decrease in advance tax [Section 210(2)]

Assessee is authorised to increase or decrease the amount of each instalment of advance tax in accordance with his estimate of his current income.

(iii) Power of Assessing Officer [Section 210(3)]

In case Assessing Officer is of the opinion that an assessee has already been assessed by way of regular assessment in respect of his income and has not deposited the advance tax during the financial year, he may order such assessee in writing, at any time during the relevant previous year but not later than 1st February, to deposit the advance tax calculated in the manner specified in section 209(2).

(iv) Amendment of order issued u/s 210 (3) [Section 210(4)]

In case Assessing Officer finds that assessee has filed a return u/s 139 (1) or u/s 142(1) or a regular assessment is made, for a previous year later than that referred in point (iii) above, he may make an amended order asking the assessee to deposit the amount of advance tax calculated on the basis of total income returned in such return or assessed on regular assessment.

(v) Assessee to intimate for reduction/increase in advance tax [Section 210(5)]

In case an assessee is served with a notice u/s 210(4) asking him to deposit amount of advance tax and in his estimation the advance tax payable on current income would be less than the amount so required to be deposited, he may intimate to the Assessing Officer to that effect and deposit that percentage of advance tax based on his own estimates. Same rule is applicable, if in his estimation, assessee finds that his current income shall be more than the income taken into consideration by the Assessing Officer and tax shall be paid in accordance with advance tax calculated on such estimated total income [210(6)].

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Instalments of Advance Tax and Due Dates [Section 211]

According to Section 211, advance tax shall be payable by all assessees who are liable to pay tax in three equal instalments on the following dates during the previous year, namely:

TABLE

A. For Company Assessee [with effect from 1.4.94]

Due date of Instalment	*Amount Payable*
(*i*) On or before 15th June	Not less than 15% of such advance tax.
(*ii*) On or before 15th September	Not less than 45% of such advance tax less any amount paid in the 1st instalment.
(*iii*) On or before 15th December	Not less than 75% of such advance tax less any amount paid in 1st and 2nd instalment.
(*iv*) On or before 15th March	Whole of amount of advance tax less amount deposited in earlier instalments.

B. For all other Assessees

Due date of Instalment	*Amount Payable*
(*i*) On or before the 15th September	(*i*) Not less than 30% of such advance tax.
(*ii*) On or before the 15th December	(*ii*) Not less than 60% of such advance tax as reduced by amount paid in earlier instalment.
(*iii*) On or before the 15th March	(*iii*) Whole amount of such advance tax as reduced by the amount, if any, paid in earlier instalment or instalments.

In case any amount of tax is deposited before 31st March, such tax shall also be treated as advance tax paid during the financial year ending on that day.

In case an order of Assessing Officer is received after any due date of instalment, the whole of the amount of the advance tax shall be payable on or before each of such date as fall after the date of service of the notice of demand.

Interest Payable by Government [Section 214]

Under Section 214, in case any assessee pays advance tax more than the amount of assessed tax determined on regular assessment, the Central Government, shall pay simple interest@ 15% to such assessee on the above said excess payment of advance tax. Such interest shall be calculated from 1st April next following the said financial year to the date of regular assessment.

It is further provided that in respect of any amount refunded on a provisional assessment u/s 141 A, no interest shall be paid for any period after the date of such provisional assessment.

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The interest paid to the assessee u/s 214 is liable to tax as income.

In case of regular assessment the amount of income on which interest was paid is reduced, the interest shall also be reduced accordingly and excess of interest paid, if any, shall be deemed to be tax payable by assessee. [Section 214 (1A)].

When any refund has been made on the assessee, the interest shall be payable only upto the date of which refund was made. [Section 214(2)]

Interest Payable by Assessee [Sec. 215]

When an assessee makes an estimate of his income himself and pays advance tax accordingly, the assessee has to pay simple interest @ 15% in case his estimate turns out to be too low and advance tax paid is less than 75% of assessed tax (in case of companies $83^1/_3$% of assessed tax) (calculated according to regular assessment).

Section 214 (2) provides that where before the date of completion of regular assessment, tax is paid by the assessee on self-assessment or otherwise—

(*i*) interest shall be calculated in accordance with the foregoing provision upto the date on which tax is so paid; and

(*ii*) thereafter interest shall be calculated on the amount by which the tax so paid (insofar as it relates to income subject to advance tax) falls short of assessed tax.

Under Section 215(3), where under any of the provisions of this Act, the amount of tax payable is reduced, the interest shall be reduced accordingly and the excess interest paid, if any, shall be refunded.

Section 215(4) says that in such case and under such circumstances as may be prescribed, the Assessing Officer may reduce or waive the interest payable by the assessee under this section.

Interest Payable by Assessee in case of Underestimate [Sec. 216]

Under Section 216, where the Assessing Officer finds that any assessee has:

(*i*) underestimated the advance tax payable by him and thereby reduced the amount payable in either of the first two instalments;

(*ii*) that he has wrongly deferred the payment of advance tax on a part of his income.

Assessing Officer may direct the assessee to pay simple interest @ 15% on the difference between the amount paid in each instalment and the amount which should have been paid.

For the purposes of this Section, an instalment due before the expiry of six months from the commencement of the previous year in respect of which it is so to be paid shall be deemed to have become due 15 days after the expiry of the said 6 months.

Interest Payable when no Estimate is made [Sec. 217]

Section 217(1) provides that where a person is not previously assessed and if he fails to submit the estimate of his income as required, simple interest @ 15% shall be charged from him. Such interest shall be charged from 1st April next (1st April of the assessment year) following the financial year in which the advance tax was payable upto the date of regular assessment.

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Under Section 217 (1A) where on making the regular assessment, the Assessing Officer finds that any such person as is referred to in Section 212(3A) has not sent the estimate referred to therein, simple interest @ 15% p.a. from the first day of April next following the financial year in which the advance tax was payable (in accordance with the sub-section) up to the date of regular assessment shall be payable by the assessee upon the amount by which advance tax paid by him falls short of the assessed tax.

Provisions of Section 215(2), 215(3), 215(4) shall also apply here.

Interest on default in payment of Advance tax [Section 234B]

1. In case an assessee, who is liable to pay advance tax u/s 208 has failed to pay such tax or where the advance tax paid u/s 210 is less than 90% of the assessed tax, the assessee shall be liable to pay simple interest at the rate of 2% for every month or a part of the month of default. The interest will be calculated from 1st day of April of the assessment year to the date of determination of regular assessment u/s 143(1).

   Interest will be calculated on an amount equal to assessed tax or the amount by which advance tax paid falls short of the assessed tax. Assessed tax means—

   (*i*) when interest is to be calculated on tax payable u/s 140A, the tax on total income as declared in the return;

   (*ii*) in any other case determined u/s 143(1) or on regular assessment. Tax as assessed above shall be reduced by the amount of tax which has been deducted or collected at source. Tax so assessed shall not include additional income tax payable u/s 143(1A). In case assessment is made for the first time u/s 147, the assessment so made shall be treated as regular assessment.

2. In case any amount of tax has been paid u/s 140A (i.e. on self-assessment) the interest shall be calculated as follows :

   (*i*) Interest shall be calculated on the amount to tax as per provisions above but it will be reduced by amount of interest paid u/s 140A and it will be calculated upto the date of payment of tax u/s 140A.

   (*ii*) From the date of payment of tax u/s 140A onwards the interest shall be calculated on the amount of assessed tax as reduced by tax deposited u/s 140A.

3. In case tax liability of assessee is increased due to assessment u/s 147; the assessee shall be required to pay interest @ 2% per month or part of the month for the period from date of regular assessment till the date of reassessment or recomputation of tax u/s 147. It till be calculated only on that much amount which is the difference between tax on reassessment u/s 147 and tax assessed on regular assessment u/s 143(1).

4. In case there is an increase in amount of interest due to reassessment u/s 154, 155, 254, 260, 262, 263, or 264, or due to order of Settlement Commission u/s 245 D(4), a demand notice shall be issued by Assessing Officer and shall be deemed as notice u/s 156 of the Act.

   In case there is reduction in the amount of interest due to reassessment under aforesaid sections, refun.1 shall be made.

5. These provision have become applicable from assessment year 1989-90 onwards.

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Interest on deferment of Advance tax [Section 234 C]

1. In case an assessee who is liable to pay advance tax u/s 208 has failed—
   (*i*) to pay advance tax; or
   (*ii*) to pay required percentage of advance tax by fixed dates; he shall be liable to pay interest @ $1^1/_2$% per month of the short fall for a period of 3 months on the amount of short fall of the advance tax. This provision shall not be applicable in case such short fall is due to under estimation of amount of capital gain or casual income as given u/s 2 (24) (ix) and the assessee pays advance tax on such income also before 31st March of the financial year.
2. In case there is short fall in payment of advance tax due to change in rates of depreciation or rate of surcharge as increased by the Finance Act 1990 or as amended by the Taxation Laws (Amendment) Act 1991, the interest as given in (1) above shall not be payable if advance tax was paid as fixed in these Acts.

This provision has been omitted with effect from 1-4-1997 *i.e.* assessment year 1997-98.

INTEREST ON DEFERMENT OF ADVANCE TAX—CORPORATE ASSESSEES [Section 234 (1)(a)]

If advance Tax Paid upto	*Rate of Interest and Period*	*Amount on Which Interest is to be Calculated*
June 15, of Assessment year is less than 12%	Simple interest @ 1.5% p.m. for 3 months	Difference between 15% of advance tax and tax so deposited
Sept. 15, of Assessment year is less than 36%	—Do—	Difference between 45% of advance tax and tax so deposited upto Sept. 15
Dec. 15, of Assessment year is less than 75%	—Do—	Difference between 75% of advance tax and tax so deposited upto Dec. 15
March 15, of Assessment year is less than 100%	—Do—	Difference between 100% of advance tax and tax deposited upto 15th March

INTEREST ON DEFERMENT OF ADVANCE TAX—NON-CORPORATE ASSESSEES [Section 234(1) (b)]

If Advance tax paid upto	*Rate of Interest and period*	*Amount on which interest is to be calculated*
15th Sept. of the Assessment year is less than 30%	Simple interest @ 1.5% p.m. for 3 months	Difference between 30% of advance tax and tax so deposited
15th December, of the Assessment year is less than 60%	—Do—	Difference between 60% of advance tax and tax so deposited upto 15th Dec.
15th March, of the Assessment year is less than 100%	Simple interest @ 1.5% p.m. for the period between 15th March and date of payment of tax	Difference between 100% of advance tax and tax so deposited upto 15th March

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Assessee deemed to be in default [Section 218]

In case the assessee fails to deposits the amount of instalment of advance tax which he is required to pay under the orders of Assessing Officer on the due date on which such instalment was due, such assessee shall be deemed to be assessee-in-default in respect of such instalment or instalments.

Credit of Advance Tax [Section 219]

Any sum, other than a penalty or interest paid by or recovered from an assessee as advance tax, shall be treated as a payment of tax in respect of the income of the period which would be the previous year for an assessment year next following the financial year in which it was payable and credit, therefore, shall be given to the assessee in the regular assessment.

QUESTIONS

1. What is tax deducted at source and give its importance ?
2. State briefly the law relating to deduction of tax at source. *[B.Com. (Hons.) Delhi]*
3. Explain in brief the provision of Income-tax law relating to 'Advance payment of Tax'. *[B.Com. Punjab]*
4. What are the provisions relating to deduction of tax at source from income chargeable under the head 'Salaries' and income from 'Dividends' ? *[B.Com. (Hons.) Delhi]*
5. What are the provisions of law regarding deduction of tax at source in respect of income from (*a*) Salaries, (*b*) Interest on Securities ? *[B.Com. Punjab, Delhi]*
6. Describe briefly two provisions of Income-tax Act for deduction of tax at source. What is the penalty for failure to deduct tax or after deduction not paying it to government account ? *[M.Com. Calicut, Andhra]*

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4 RECOVERY OF TAX AND REFUNDS

Payment of tax—Penalty payable for tax in default—Modes of recovery of tax—Tax recovery officer— Other modes—Tax clearance certificate—Restriction on registration of transfers—Refunds—Questions.

PAYMENT OF TAX

When is Tax Payable ? [Section 220 (1)]

Any amount otherwise than by way of advance tax, shall be payable within 30 days of service of the notice of demand. All the assessees who are served with such notices must deposit such amount which is written in the notice and at the place and to the person mentioned in the notice.

But where the Assessing Officer has any reason to believe that it will be detrimental to revenue if the full period of 30 day is allowed, he may but with previous approval of the Deputy Commissioner, reduce the number of days which shall be less than 30 days and may be specified by him in the notice of demand.

Payment of Interest

If the amount specified in the notice is not paid within the specified time, the assessee shall be liable to pay simple interest @ 1½% per month from the day commencing after the end of the period mentioned in the notice. If due to any reason (rectification of error, appeal etc.) the amount of tax had been reduced, the interest shall be reduced accordingly and the excess interest paid, if any, shall be refunded. [Section 220 (2)].

Extension of date

The Assessing Officer is empowered to extend the date of payment of tax if he is approached by the assessee with an application before the due date. The Assessing Officer may also allow the payment to be made in instalments subject to such conditions as he may think fit under the circumstances of the case. However, interest shall be charged in such a case and it will be calculated from the date specified in the notice of demand. [Section 220 (3)].

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Assessee in default

The assessee shall be considered to be an assessee in default if he fails to pay tax within the time allowed originally or extended and to the person and place mentioned in the notice. The assessee cannot be treated as being in default unless a notice of demand has been duly served. [Section 220 (4)]

Payment of tax in instalments

The assessee may be allowed to pay the tax in instalments and if the assessee commits default in paying any one of the instalments within the time specified, the assessee shall be deemed to be in default as to the whole of the amount then outstanding, and the other instalment or instalments shall be deemed to have been due on the same date as the instalment actually in default. [Section 220 (5)].

Assessee deemed to be not in default

U/s 220 (6), whereas assessee has presented an appeal u/s 246, the Assessing Officer may at his discretion and subject to such conditions as he may think fit to impose in the circumstances of the case, treat the assessee as not being in default in respect of the amount in dispute in the appeal, even though the time for payment has expired, as long as such appeal remains undisposed of.

Under Sec. 220 (6), if the assessee has filed an appeal against the assessment made by the Assessing Officer the filing of the appeal would not by itself enable the assessee to withhold payment of the tax in dispute. *[Union of India v. Nawn 84 ITR 526]*. But this section empowers the Assessing Officer that he may, in his discretion, treat the assessee as not being in default in respect of the amount in dispute in the appeal as long as such appeal remains undisposed of. The Assessing Officer can exercise the power only during the pendency of an appeal before the Deputy Commissioner (Appeals) against the assessment made by him. *[C.I.T. v. Mohanlal Gokuldas 95 I.T.R. 537]*. The exercise of this power by the Assessing Officer is a quasi-judicial function and cannot be controlled by the Commissioner but it must be used by the Assessing Officer fairly and reasonably and not arbitrarily or capriciously *[Hardeodas, Jagan Nath vs I.T.O. 43 I.T.R. 526]*.

Section 220 (7) provides that where an assessee has been assessed in respect of income arising outside India in a country the laws of which prohibit or restrict the remittance of money to India, in such cases the Assessing Officer shall not treat the assessee in default in respect of income which the assessee cannot bring into India due to such restrictions. The assessee shall not be treated in default in respect of such part of the tax until the prohibition or restriction is removed.

If is further provided in the explanation attached to this Section that for the purposes of this Section, income shall be deemed to have been brought into India if it has been utilised or could have been utilised for the purpose of any expenditure actually incurred by the assessee outside India, or if the income, whether capitalised or not has been brought into India in any form.

Penalty Payable when Tax is in Default [Section 221]

When an assessee is in default or is deemed to be in default in making payment of tax, he shall, in addition to the amount of the arrears and the amount of interest

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payable u/s 220 (2), be liable by way of penalty. The amount of the penalty will be according to the desire of the Assessing Officer and in case of continued default the amount of penalty can *go upto the amount of tax in arrears.*

This section expressly provides that the assessee shall be given a reasonable chance of being heard before imposing this penalty.*[J.K. Iron & Steel Co. Ltd. v. C.I.T. 63 I.T.R.79]*

Where the Assessing Officer is satisfied that the default was for good and sufficient reasons, no penalty shall be liable under this section.

A penalty under this section cannot be imposed unless a notice of demand has been served on the assessee, since the assessee who is not served with a notice of demand cannot be said to be in default if he does not pay the tax.

The assessee shall not cease to be liable to any penalty merely by reason of the fact that before the levy of such penalty, he has paid the tax. [221 (1) Explanation.]

Whereas as a result of any final order, the amount of tax on which penalty was levied, has been wholly reduced, the penalty levied shall be cancelled and amount of penalty paid shall be fully refunded. [Section 221 (2)]

MODES OF RECOVERY OF TAX

Section 222 provides that in case assessee fails to pay any sum imposed by way of interest, fine, penalty or any other sum payable under the provisions of this Act, the same shall be recoverable in the manner specified in the Act for the recovery of arrears of tax.

"Tax Recovery Officer" means

(*i*) A Collector or an Additional Collector;

(*ii*) Any such officer empowered to effect recovery of arrears of land revenue or other public demand under any law relating to land revenue or other public demand for the time being in force in the State as may be authorised by the State Government, by general or special notification in the Official Gazettee, to exercise the powers of a Tax Recovery Officer;

(*iii*) Any Gazetted Officer of the Central or a State Govt. who may be authorised by the Central Govt., by general or special notification in the Officer Gazette, to exercise the powers of a Tax Recovery Officer.

When an assessee is in default or is deemed to be in default in making a payment of tax, the Tax Recovery Officer may draw up under his signatures a certificate in the prescribed form specifying the amount of arrears due from the assessee and shall proceed to recover from such assessee the amount specified in the certificate by one or more of the modes mentioned below in accordance with the rules laid down in the Second Schedule:

(*a*) attachment and sale of the assessee's movable property;

(*b*) attachment and sale of the assessee's immovable property;

(*c*) arrest of the assessee and his detention in prison;

(*d*) appointing a receiver for the management of the Assessee's movable and immovable properties.

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Explanation. For the purposes of this sub-section, the assessee's movable or immovable property shall include any property which has been transferred, directly or indirectly on or after the 1st day of June, 1973, by the assessee to his spouse or minor child or son's wife or son's minor child, otherwise than for adequate consideration, and which is held by, or stands in the name of, any of the persons aforesaid and so far as the movable or immovable property so transferred to his minor child or his son's minor child is concerned it shall, even after the date of attainment of majority by such minor child or son's minor child, as the case may be, continue to be included in the assessee's movable or immovable property for recovering any arrears due from the assessee in respect of any period prior to such date.

The Tax Recovery Officer may take action u/s 222(1) notwithstanding the proceeding for recovery of the arrears by any other mode being taken.

Section 223 empowers the Assessing Officer to send such a certificate to a Tax Recovery Officer in whose jurisdiction the assessee carries on his business or resides or is having property.

Tax Recovery Officer by whom recovery is to be effected [Sec. 223]

The Tax Recovery Officer competent to take action shall be—

(*a*) The Tax Recovery Officer within whose jurisdiction the assessee carries on his business or profession or within whose jurisdiction the principal place of his business or profession is situated, or

(*b*) The Tax Recovery Officer within whose jurisdiction the assessee resides or any movable or immovable property of the assessee is situated.

Jurisdiction to the Tax Recovery Officer is assigned under the orders or directions issued by the Board, or by the Chief Commissioner or Commissioner who is authorised by the Board in this regard.

Where the assessee has property within the jurisdiction of more than one Tax Recovery Officer and T.R.O. who has drawn the certificate is not able to recover the entire amount of tax due against assessee by sale of the property (movable or immovable) within his jurisdiction he may send the certificate or a copy of the certificate if only a part of the amount to be recovered to a Tax Recovery Officer within whose jurisdiction the assessee resides or has property. On receipt of such a certificate specifying the amount to be recovered, the Tax Recovery Officer will proceed to recover the amount.

Validity of Certificate and Cancellation or Amendments thereof [Sec. 224]

Once a certificate has been drawn by the T.R.O., it shall not be open to the assessee to dispute the correctness of the certificate on any ground whatsoever. But in case T.R.O. thinks fit to correct any clerical or arithmetical mistake therein, the cancellation of certificate is necessary, then he is empowered to do so.

Stay of Proceedings in pursuance of Certificate and Amendment or Cancellation thereof [Sec. 225]

It shall be lawful for the T.R.O. to grant time for payment of any tax and when he does so, he shall stay the proceedings for the recovery of such tax until the expiry of the time so granted.

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Where on an appeal and other proceedings under the act, the demand on Tax (for which the certificate regarding recovery has been drawn and as a consequence of appeal etc.) has been reduced but the other is the subject-matter of further proceeding under the Act, the Tax Recovery Officer shall stay the recovery of such part of the amount for the period for which the appeal or other proceedings remain pending.

Where a certificate for the recovery of the tax was drawn but later on the amount of the outstanding tax demand is reduced as a result of an appeal or other proceeding, the T.R.O. shall amend the certificate or cancel it, as the case may be, after the appeal or other proceeding has become final and conclusive.

Other Modes of Recovery [Sec. 226]

Where no certificate has been drawn (by the Tax Recovery Officer) u/s 222, the Assessing Officer may recover the tax by any one or more of the modes provided in this section.

Where a certificate has been drawn (by the Tax Recovery Officer) u/s 222, the Assessing officer may recover the tax by any one or more of the modes provided in this section.

(i) Deduction from salary

Under Section 226 (2), if the assessee is in receipt of any income under the head 'Salary', the Assessing Officer or T.R.O. may approach such person paying salary to deduct arrears of tax from the salary of the assessee and such person shall comply with any such requisition and shall pay the sum so deducted to the credit of Central Government or as the Board directs.

But any part of the salary exempt from attachment in execution of degree of a civil court, shall be exempt from any requisition made under this sub-section.

(ii) Collection from Persons who owe Money to Assessee

Under Section 226 (3) the Assessing Officer or T.R.O. may, at any time or from time to time, by notice in writing require any person from whom money is due or may become due to the assessee or any person who holds or may subsequently hold money for or on account of the assessee; to pay to the Assessing Officer or T.R.O. (when the money becomes due) the amount which may be sufficient to cover the amount due from the assessee.

Under the provision of this section, the Assessing Officer or T.R.O. can require any other person, who owes any amount to the assessee, to pay the amount to the Assessing Officer or T.R.O. to cover the arrears of tax due from an assessee. This type of notice can be issued to a post office, banking company, insurance company etc. Every person to whom such a notice is issued, shall be bound to comply with such notice. The Assessing Officer or T.R.O. shall grant a receipt for any amount paid in compliance with such a notice.

If a person, to whom such notice is issued, fails to comply with, he shall be personally liable to the Assessing Officer or T.R.O. to the extent of his own liability to the assessee so discharged or to the extent of the assessee's liability for any sum due under this Act, whichever is less and such person shall be treated as assessee-in-default.

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In case the person to whom a notice is served under this section does not deny his liability to the assessee, and he fails to make the payment to the Assessing Officer or T.R.O. such a person would be deemed to be an assessee-in-default and recovery proceedings may be taken against him for realisation of the amount as if it were an arrear or tax due from him.*[Lakshmi Commercial Bank Ltd. vs. Dharam Singh 94 I.T.R. 416, 423].*

Further where such a person makes a payment to the assessee in disregard to the notice sent to him, such a person would be personally liable for the amount of the payment made by him to the assessee or to the extent of the amount of tax or other sum due from such an assessee, whichever is less.

Any person who declares on oath that sum demanded by that notice is not due to the assessee, cannot be compelled to make payment but if later on it is discovered that he made a false statement, he would be personally liable to the Assessing Officer or T.R.O. to the extent of his own liability to the assessee or assessee's tax liability under this Act, whichever is less *(Southern Textiles Ltd. vs. I.T.O. 83 I.T.R. 790).* Any person making false statement under this section may also be liable to prosecution u/s 277.

It may also be noted that before a notice under this section is served, the Assessing Officer or T.R.O. should ensure that on date of the service of the notice, such a person should be under an existing liability to pay an amount to the assessee *(P.K. Trading Co. vs. I.T.O 87 I.T.R. 427)* . So a notice under this sub-section cannot be served on a debtor of a suspected benamidar of the assessee. Thus the existence of liability towards the assessee is a must.

(iii) Application to Court for Payment of Money in Court's Custody

Under Section 226 (4), the Assessing Officer or T.R.O. may apply to the court in whose custody there is money belonging to the assessee for payment to him of the entire amount of such money, or if it is more than the tax due, an amount sufficient to discharge the tax.

(iv) Distraint and Sale of Movable Property

Under Section 226 (5), the Assessing Officer or T.R.O. may if so authorised by the Chief Commissioner or the Commissioner by general or special order, recover any arrears of tax due from an assessee by distraint and sale of his movable property in the manner laid down in the Third Schedule.

(v) Recovery through State Government

Under Section 227, if the recovery of tax in any area has been entrusted to State Government, the State Government may direct that tax shall be recovered from the assessee along with other taxes (i.e., municipal tax or local rate). Such tax shall be collected by the same person and in the same manner as the municipal tax or local rate is recovered.

Recovery of tax in Pursuance of Agreements with Foreign Countries [Section 228 A]

If Central Govt. is having an agreement with the government of a foreign country for recovery of income-tax under this Act and the corresponding law in force in that country and the Government of the country or any authority under the

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Government which is specified in this behalf in such agreement, sends to the Board a certificate for the recovery of any tax due under such corresponding law from a person having any property in India, the Board may forward such certificate to any T.R.O. within whose jurisdiction such property is situated.

(*a*) On receipt of such certificate, the T.R.O. shall proceed to recover the amount specified in the certificate in the manner in which he would proceed to recover the amount specified in a certificate drawn by him u/s 222.

(*b*) Remit any sum so recovered by him to the Board after deducting his expense in connection with recovery proceedings [u/s 228 A (1)]. U/s 228 A (2) where an assessee is in default or deemed to be in default in making a payment of tax, the T.R.O. may, if the assessee has property in a foreign country, forward to the Board a certificate drawn up by him u/s 222 and the Board may take such action thereon as it may deem appropriate having regard to the terms of the agreement with such country. The foreign country must be such with which the Central Govt. has entered into an agreement for the recovery of income-tax under this Act and corresponding law in force in that country.

Recovery of Penalties, Fine, Interest and other Sums [Sec. 229]

Any sum imposed by way of interest, fine, penalty or any other sum payable under the provisions of this Act, shall be recoverable in the manner provided in this chapter for the recovery of arrears of tax.

Issue of Tax clearance Certificate [Section 230]

1. In case a person is domiciled in India at the time of his departure from India and he—
   - (*i*) intends to leave India as emigrant; or
   - (*ii*) intends to proceed to another country on a work permit with the object of taking up employment or other occupation in that country; or
   - (*iii*) in respect of whom circumstances exist, which, in the opinion of an income-tax authority, render it necessary for him to obtain a certificate under this section;

   he shall not leave the territory of India by land, air, or sea unless he obtains, from such authority as is appointed by central Govt. a certificate stating that he has no liability under
   - (*a*) the Income-tax Act 1961;
   - (*b*) the Income-tax Act 1922;
   - (*c*) the Excess profits tax Act 1940;
   - (*d*) the Wealth tax Act 1957;
   - (*e*) the Expenditure-tax Act 1957; or
   - (*f*) the Gift-tax Act 1958

   or he has made satisfactory arrangements for the payment of all or any of such taxes which are or may become payable by such person.
2. In case of persons not domiciled in India the above provisions are applicable in same manner but the competent authority may issue such certificate in respect of single journey or in respect of all journeys

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undertaken by such person within prescribed period as prescribed in certificate, provided such person intends to return to India.

3 In case a ship or aircraft owner allows any person to leave India without satisfying himself about the certificate, such owner shall be personally liable for the amount of tax payable by such person.

Restriction on Registration of transfers of Immovable assets in certain cases [Section 230A]

(1) In case any document is required to be registered on transfer, assignment, limiting or extinguishing any right, title or interest of any person in any property and the value is more than Rs. 5 lakh, the registering officer shall not register such document unless a certificate is obtained from the Assessing Officer certifying that such person has paid or made satisfactory provision for payment of all existing liabilities under any of the following Acts:

(*i*) the Income Tax Act 1961;
(*ii*) the Income-Tax Act 1922;
(*iii*) the Excess Profits Tax Act 1940;
(*iv*) the Business Profits Tax Act 1947;
(*v*) the Wealth tax Act 1957;
(*vi*) the Expenditure Tax Act 1957;
(*vii*) the Gift tax Act 1958;
(*viii*) the Super Profits Tax Act 1963; or
(*ix*) the Companies profits Sur tax Act 1964.

or, the registration of document shall not effect the recovery of any liability under the aforesaid Acts.

2. The application for such certificate shall be submitted by such person in prescribed form and in prescribed manner.
3. These provisions shall not be applicable where the person as referred above, is an institution, association or body or asset belongs to an institution, association or body which the Board may notify in Official Gazette.

Recovery by suit [Sec. 232]

The Assessing Officer's efforts to recover the arrears through different modes of recovery specified in this chapter shall not affect in any way—

(*a*) any other law for the time being in force relating to the recovery of debts due to Government; or

(*b*) the right of the Government to institute a suit for the recovery of the arrears due from the assessee.

This means the Government or the Assessing Officer as the case may be, is free to take a recourse to any such action, or suit, notwithstanding that the tax due is being recovered from the assessee by any mode specified in this chapter. This further explains that the modes of recovery provided by this Act are not exhaustive and the Government continues to enjoy the right of enforcing payment by any other method open to it. *[Manickam Chettiar vs. I.T.O. 6 I.T.R.180]*

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REFUNDS

If, in any assessment year an assessee pays the tax which is more than the amount for which he is actually chargeable and if the assessee proves excess payment before the Assessing Officer, section 237 empowers the assessee to claim a refund of the excess. Once the Assessing Officer is satisfied about the excess payment made by the assessee, he can allow the claim or refund.

Under the following cases a claim to refund may arise—

1. When tax is deducted at source from salary, interest on securities or debentures, dividends at a rate higher than the rate applicable to the total income of an assessee.
2. When tax paid in advance exceeds the amount of tax actually payable as determined at the time of regular assessment.
3. When on appeal against Assessing Officer's assessment or on revision of the assessment, the higher authorities reduce the taxable income determined by the lower authority.
4. When tax calculated was higher due to some mistake and later on tax liability is reduced on account of rectification of a mistake.
5. When tax was calculated at the higher rate on the payment given to non-residents whereas they were actually chargeable at a lower rate of income-tax.
6. When due to double taxation, the assessee is entitled to a double taxation relief.

Who is Allowed to Claim Refund ?

Under Section 238 (1), where the income of one person is included in the total income of any other person, the later alone shall be entitled to refund in case of excess payment of tax in this case.

In the case of death, incapacity, insolvency, liquidation etc. the assessee is unable to claim refund, section 238(2) allows the legal representative, trustee, guardian or receiver of such assessee to claim or receive such refund for the benefit of such assessee or his estate.

A claim for refund must be filed in the prescribed form and verified in the prescribed manner. Rule 41 of Income Tax Rules, 1962 lays down that a claim for refund shall be made in Form No. 30. In case the claimant of refund has not filed the return of his income, the form for refund shall be accompanied by a return of his income. Where any part of the total income of a person claiming refund consists of dividends or any other income from which tax is deducted at source, the claim for refund shall be accompanied by a certificate which is issued by the tax-deducting authority. The claim for refund may be presented personally by the claimant or through an agent or may be sent by post.

Time Limit for Claiming Refund

The claim for refund cannot be allowed unless it is presented within the time prescribed in Section 239 (2).

(*i*) where the refund relates to the assessment years upto 1967-68, four years from the last day of such assessment year.

(*ii*) In case the refund claim relates to the assessment years 1968-69, three years from the last day of the assessment year.

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(*iii*) Refund claims relating to the assessment years after 1968-69 *one year* from the last day of such assessment year.

Refund on Appeal etc. [Section 240]

Where due to the orders of the court in an appeal or other proceedings, refund of any amount becomes due to the assessee the Assessing Officer shall refund the amount to the assessee without his having to make any claim in that behalf.

It is further provided that where—

(*a*) an assessment is set aside or cancelled and an order of fresh assessment is directed to be made, the refund, if any, shall become due only on the making of such fresh assessment;

(*b*) the assessment is annulled, the refund shall become due only of the amount, if any, of the tax paid in excess of the tax chargeable on the total income returned by the assessee.

Power to withhold Refund [Section 241]

Where refund for any amount becomes due to assessee as a result of an order u/s 143(1) or any other section and Assessing Officer is of the opinion that due to reasons of—

(*a*) a notice has been issued or is likely to be issued in respect of return filed; or

(*b*) the order is the subject-matter of an appeal or further proceedings; or

(*c*) any other proceeding under this Act is pending.

where the grant of refund effects the revenue adversely, he may, after the prior approval of Chief Commissioner or Commissioner withhold the refund till such time as the Chief Commissioner or Commissioner permits.

Correctness of Assessment not to be Questioned [Section 242]

In case of final and conclusive assessment the assessee cannot question it or ask for its revision. He shall not be entitled to any relief on such claim except refund of tax wrongly paid.

Under Sec. 242, the assessee cannot both apply for a refund and at the same time question the correctness of the finalised assessment giving rise to the refund. It has been held in a case *C.I.T. vs. The Tribune Trust 16 I.T.R. 214 222, 224 (P.C.)* that if an assessment is not correct or is unjustified according to the law and tax has been paid accordingly, the assessee's remedy is to go in appeal against the assessment and not to apply for a refund.

Interest on Delayed Refunds [Section 243]

Simple interest @ 15% p.a shall be payable to the assessee by the Central Government on the delayed refunds. Delayed refunds refer to the refund which is not granted by the Assessing Officer within the specified time. The specified time is as under:

Section 243 states that where the total income of the assessee does not consist solely of income from interest on securities or dividend, the Assessing Officer should grant the refund within 3 months of the end of the month in which the total income is determined (under the provisions of this Act).

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In any other case, the refund should be made within three months of the end of the month in which the claim for refund is made.

So, if the refund is not granted within the above-mentioned time-period, the Central Government shall pay to the assessee simple interest @ 15% on the amount directed to be refunded from the date immediately following the expiry of the period of three months to the date of the order granting the refund.

If the delay was caused due to any reason for which assessee is responsible, directly or indirectly, the period for which assessee is responsible shall be excluded from the period for which interest is payable.

If there is any dispute about the said period the matter will be referred to the Chief Commissioner or the Commissioner whose decision in this regard shall be final.

Interest on Refund Where no Claim is Needed [Section 244]

The Assessing Officer should grant the refund even without any claim being made by the assessee in a case where refund is due to the assessee under an order made u/s 240 (in an appeal). The simple interest @ 15% shall be allowed on the delayed refund.

Where the whole or any part of the refund referred to in sub-section (1) is due to the assessee, as a result of any amount having been paid by him after the 31st day of March, 1975, in pursuance of any order of assessment of penalty and such amount or any part thereof having been found in appeal or other proceeding under this Act to be in excess of the amount which such assessee is liable to pay as tax or penalty, as the case may be, under this Act. The Central Government shall pay to such assessee simple interest at the rate specified in sub-section (1) on the amount so found to be in excess from the date on which such amount was paid to the date on which the refund is granted.

Provided that, where the amount so found to be in excess was paid in instalments, such interest shall be payable on the amount of each such instalment or any of such instalments, which was in excess, from the date on which such instalment was paid to the date on which the refund is granted.

Provided further that no interest under this sub-section shall be payable for a period of one month from the date of the passing of the order in appeal or other proceedings.

Provided also that where any interest is payable to an assessee under this sub-section, no interest under sub-section (1) shall be payable to him in respect of an amount so found to be in excess.

Under Section 244 (2) where a refund is withheld under the provision of Section 241, the Central Government shall pay interest @ 15% on the amount of refund ultimately determined to be due as a result of the appeal or further proceeding for the period commencing after the expiry of three months from the end of the month in which the order referred to in Section 241 is passed to the date the refund is granted.

In case where the assessment was set aside by an appellate authority and a direction issued to make at a fresh assessment, interest shall be payable on the amount of refund becoming due as a result of assessment being set aside and the interest is payable upon the expiry of 3 months period to be calculated from the appellate order and not the fresh assessment order *(Purshottam Dayal Varshney v. C.I.T. 94 I.T.R. 187)*.

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The above provisions given u/s 244(1), 244 (2) or 244 (3) are applicable only on assessments relating to the period prior to 1-4-89. From Assessment year1989-90 the new provisions are given u/s 244 A.

Interest on Refund [Section 244A]

Interest shall be paid to assessee where—

(*a*) refund is out of any tax deducted at source or advance tax paid during the financial year preceding the assessment year @ 1% for every month or part of the month from 1st April till the date on which refund is granted.

No interest shall be payable if the amount of refund in less than 10% of tax determined u/s 143 (1).

(*b*) refund is due in any other case the interest @ 1% per month or part of the month thereof, shall be calculated from the date of payment of such tax or penalty till the date refund is made.

(2) In case delay in refund is due to fault of assessee, the Chief Commissioner or the Commissioner may exclude the period of such delay for calculating interest on refund.

(3) In case reassessment or recomputation of income is made u/s 143 (3), 144, 147, 154, 155, 250, 254, 260, 262, 263, or 264 or under order of settlement Commission u/s 245 D (4) and the amount of interest is reduced, the demand notice for such amount shall be issued and it shall be deemed to be a notice u/s 156.

Set-of Refunds against Tax Remaining Payable [Section 245]

Section 245 lays down that if in an assessment year, a refund is due to an assessee, the same may be adjusted against the payment of tax due against the same assessee in another assessment year. If a part of the refund is utilised in setting of against tax remaining payable by the assessee, the balance shall be refunded. Wherever this type of adjustment is made, the assessee is duly intimated in writing of the action proposed to be taken under this section.

QUESTIONS

1. State briefly the law relating to:
   (*i*) Deduction of Tax at source. (*ii*) Refunds. *[B.Com. (Hons.) Delhi]*
2. What are the circumstances in which a claim for refund of tax may arise ? Describe briefly the procedure of claiming a refund.
3. Explain in brief the provisions of income-tax law relating to 'Advance payment of tax'. *[B.Com. Punjab]*
4. What are the provisions relating to deduction of tax at source from income chargeable under the head 'Salaries' and income from 'Dividends' ? *[B.Com. (Hons.) Delhi]*
5. What are the provisions of law regarding deduction of tax at source in respect of income from (*a*) Salaries, (*b*) Interest on Securities? *[B.Com. Punjab, Delhi]*

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5 SETTLEMENT COMMISSION

Setting up—Application for settlement—Calculation of additional Income-tax—Procedure on receipt of application—Powers—Rules—Questions.

Taxation laws (Amendment) Act has brought major administrative changes in the Income-tax Act. One of these changes is the setting up of Income-tax Settlement Commission. Till now the Income-tax cases were settled on an informal basis without any statutory provision. But with the setting up of settlement commission the settlement proceedings have become a formal affair.

SETTING UP

Setting up of Settlement Commission. On the recommendations of Wanchoo Committee, the Income-tax Act, 1975 and a new Chapter XIXA— Settlement of Cases—has been added. This chapter provides for setting up Settlement Commission, procedure for application for settlement etc. In pursuance of this power, the Central Government has appointed the Settlement Commission and it has started functioning from 1st April 1976.

Constitution of Settlement Commission. (Section 245B). The Central Government has been empowered to constitute 'Income-tax Settlement Commission'. The Commission shall consist of a Chairman and as many Vice-Chairmen and other members as the Central Govt. thinks fit and shall function as the Deptt. of Central Govt. dealing with direct taxes. The Chairman, Vice-Chairmen and other members of the Commission shall be appointed from amongst persons of integrity and outstanding ability having special knowledge of and experience in problems relating to direct taxes and business accounts. Central Government can ask any two members of Central Board of Direct Taxes to act as the members of Settlement Commission and on such appointment he shall, cease to be a member of the Board.

Jurisdiction and powers of Settlement Commission [Section 245 BA]

1. The jurisdiction, powers and authority of the Settlement Commission may be exercised in Benches.
2. A Bench shall be presided over by the Chairman or Vice-Chairman and shall consist of two other members.
3. The Bench which is presided over by the Chairman shall be known as Principal Bench and other benches shall be known as additional Benches.

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4. The Chairman may authorise any of the members to discharge the functions of Vice-Chairman.
5. In case any member of the Bench is unable to discharge his duties owing to absence, illness on any other reason, the other members of the Bench may function as the Bench. The senior most member of the Bench shall act as Presiding Officer if regular presiding Officer is not present.

5A. The Chairman may, for the disposal of a particular case, constitute a special Bench consisting of more than three members.

6. Govt. may fix the places at which the Principal Bench, additional Benches and special Bench shall ordinarily sit. New Delhi, Bombay have been notified as these places.

Vice-Chairman to Act as Chairman [Section 245 BB]

In case a vacancy of Chairman arises due to death, resignation or otherwise, Central Govt. may authorise one of the Vice-Chairmen to act as Chairman till a regular Chairman is appointed. The same may be made applicable in case of a temporary vacancy arising due to absence, illness or any other cause.

The Vice-Chairman, so appointed, in the absence of permanent Chairman shall discharge the functions of the Chairman till the date on which the Chairman resumes his duties.

Transfer of Cases [Section 245 BC]

The Chairman is entitled to transfer a case from one Bench to another Bench either on an application by the assessee or the Chief Commissioner or Commissioner of his own motion without any notice.

Decision to be majority [Section 245 BD]

All the decisions of the Bench must be by majority. In the event members are equally divided, the matter shall be referred to the Chairman. He may hear the matter himself or may refer it to one or more of the other members of the Commission and then the case shall be decided by a majority decision.

Application for Settlement of Cases (Section 245 C). Any assessee against whom a case is pending before any Income-tax Authority can apply to the Settlement Commission in the prescribed manner to have the case settled. The application must be accompanied by prescribed fee and once it is submitted it cannot be withdrawn.

An assessee may, at any stage of a case relating to him, make an application in prescribed form for settlement of case. Such application must contain:

(*i*) a full and true disclosure of his income;

(*ii*) the manner in which such income is derived;

(*iii*) the additional amount of income tax payable on such disclosed income; and

(*iv*) the additional income-tax payable on such disclosed income that (calculated as per provision of 1A) exceeds Rs. 100,000 (one hundred thousand rupees)

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Calculation of additional Income-tax [245C (1A)]

The method for calculation of additional tax is given in sub-section (1B) to (1D) of section 245C. These provisions are—

A—Where the income disclosed relates to one previous year— [245 C (1B)]

(*a*) if return is not filed for such year—tax shall be calculated on such disclosed income presuming it to be total income;

(*b*) if return is filed and assessment has not been made for such year—the tax shall be calculated on total income arrived at after aggregating the total income as given in return and the disclosed income;

(*c*) if return is filed and assessment has been made—tax shall be calculated on the aggregate of assessed income and disclosed income;

(*d*) Tax so calculated shall be reduced by the amount of the tax deducted at source, advance tax paid, tax paid on self-assessment or on regular assessment as per (c) above. The resultant amount shall be called *additional Income-tax.*

B—Where the income disclosed relates to more than one previous year [245C (1D)].

The income shall be considered to be the income of each previous year and tax shall be calculated as per aforesaid provisions in respect of each previous year. The difference of tax payable and tax paid in respect of each previous year shall be calculated. The difference in amount of each previous year shall be aggregated and this amount shall be called *additional Income-tax.*

Bar on making application [245 C (1E)]

Where any books of account, other documents, money, bullion, jewellery or other valuable articles or things have been seized u/s 132 the assessee shall not be entitled to make an application for settlement before the expiry of 120 days from the date of such seizure.

Every application made under Section 245 (1) shall be accompanied by such fee as may be prescribed. An application made under section 245(1) shall not be allowed to be withdrawn by the applicant.

Procedure on Receipt of Application [Section 245D]. The Commission shall, on receipt of application call for a report from the respective Commissioner and on receipt of such report and after the consideration of all relevant material, the Commission will either allow the application to be proceeded with or reject the application. Application cannot be rejected without giving applicant an opportunity of being heard.

The Commissioner shall furnish the report within 45 days from the receipt of communication in case of all applications made on or after 1.7.1995 and if the Commissioner fails to furnish the report within the said period the Settlement Commission may make the order without such report. A copy of such orders shall be sent to the applicant and to the Commissioner.

Payment of additional Income-tax [245D (2A)]

The assessee must deposit the additional amount of tax payable within 35 days of the receipt of the copy of the order and shall submit proof of such payment to the Settlement Commission.

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In case assessee is unable to deposit the amount of tax due to good and sufficient reasons proved to the satisfaction of Settlement Commission it may permit such assessee to pay the amount of additional income-tax in instalments provided the assessee furnishes the requisite security [24D (2B)].

In case assessee fails to deposit the amount of tax within prescribed time he shall be required to pay interest @ 15% p.a. on the amount remaining unpaid from the date of expiry of the period of 35 days. [245 D (2C)].

In case of default, Settlement Commission can levy penalty and the amount of tax, interest and penalty can be recovered according to the procedure laid down for recovery of tax. [24D (2D)].

Where the Commission decides to proceed with the application, it may call for the relevant record from the Commissioner and after examining the record and after conducting further investigation may ask the Commissioner to conduct any further investigation if required. If the Settlement Commission finds that any further inquiry or investigation is required in this matter, it may direct the Commissioner to conduct or cause to conduct such further investigation and furnish a report on the matter covered by the application and furnish any further facts related to the case. [Sec. 245D(3)].

On examining the records and reports received by the Commission, it may pass such orders as it thinks fit but only after giving the applicant and Commissioner an opportunity of being heard either in person or through an authorised representative. [Sec. 245D (4)]

The materials brought on record before Settlement Commission shall be considered by the members of the concerned Bench before passing any orders. [Section 245 D (5)]

Any order passed by the Commission shall provide for the terms of settlement including any demand for the tax, penalty or interest and the manner in which any such sum due on the settlement shall be paid. The orders of the Commission must be explicit, and it shall be void if it is found afterwards that settlement was obtained by way of fraud or misrepresentation. In this situation the proceedings of the case will begin from the stage they were left when case was referred from Income-tax authorities to Settlement Commission. [Section 245D (6)]

In case any tax is payable as a result of the order of Settlement Commission and is not paid within 35 days of the receipt of such order, interest at the rate of 15% shall be payable by assessee even if the Settlement Commission has extended the time or allowed the tax to be paid in instalments. The interest will be charged from the expiry of period of 35 days. [Section 245 D (6A)]

In case settlement becomes void as provided at (6) above, and the proceedings before Income-tax authorities have begun, such authorities shall complete the proceedings at any time before the expiry of 2 years from the end of financial year in which the settlement became void [Section 245 D (7)]

The provision of section 153 shall not apply to any order of settlement and provision of section 186 (i) also shall not apply to the cancellation of registration of firm if required under directions of Settlement Commission. [Section 245 D (8)]

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Power of Settlement Commission to order provisional attachment to protect revenue [Sec. 24DD (1)]. Where, during the pendency of any proceeding before it, the Settlement Commission is of the opinion that for the purpose of protecting the interest of the revenue it is necessary so to do, it may, by order, attach provisionally any property belonging to the applicant in the manner provided in the Second Schedule:

Provided that where a provisional attachment made under section 281 B is pending immediately before an application is made under section 245 C, an order under this sub-section shall continue such provisional attachment up to the period up to which an order made under section 281 B would have continued if such application had not been made.

Provided further that where the Settlement Commission Passes an order under this sub-section after the expiry of the period referred to in the precceeding proviso, the provisions of sub-section (2) shall apply to such order as if the said order had originally been passed by the Settlement Commission.

(2) Every provisional attachment made by the Settlement Commission under sub-section (1) shall cease to have effect after the expiry of a period of six months from the date of the order made under sub-section (1);

Provided that the Settlement Commission may, for reason to be recorded in writing, extend the aforesaid period by such further period or periods as it thinks fit, so however, that the total period of extension shall not in any case exceed two years.

POWERS

(*i*) **Powers to Re-open the Completed Proceeding** [Section 245F]. With concurrence of the applicant, the Commission is empowered to re-open the completed assessments when it is necessary and expedient. The Commission has to record the reasons in writing which led it to believe that re-opening of completed assessment is necessary for the proper disposal of the case pending before the Commission. The Commission cannot re-open the assessment after the expiry of 9 years from the end of the assessment year to which such re-opening proceedings relate.

(*ii*) **Powers of Income-tax Authority** [Section 245F (1)]. The Settlement Commission shall have all the powers which are vested in an Income-tax authority. When a case is pending before the Commission, its jurisdiction shall be exclusive in relation to the case [245F (2)]. Where the Commission has not expressly directed to the contrary, the provision of self-assessment tax shall remain in force. [245 F(3)]

(*iii*) **Powers to Regulate its own Procedure** [Section 245F (5)]. The Commission has been empowered to regulate its own procedure for the settlement of the case.

(*iv*) **Inspection of Reports** [Section 24G]. For gathering relevant facts for the proper settlement of the case the Commission approaches the different Income-tax Authorities for supplying such reports and facts to the Commission. All such reports sent by the Income-tax authorities to the Settlement Commission are confidential and no person shall be entitled to inspect or obtain copies of such reports. However, the Commission is empowered and it may at its discretion, furnish copies on payment of prescribed fees and application made in this behalf.

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Where any assessee finds it necessary to rebut any evidence on record against him, the Commission must mandatorily provide the assessee with certified copies of the report from the relevant part of the report on payment of the prescribed fees and application made in this behalf.

(*v*) **Power to Grant Immunity from Prosecution and Penalty** (Section 245H). If any person who has made the application for settlement has co-operated with the Commission and has made full and true disclosure of his income, the Commission may grant such person immunity from prosecution for any offence or also from imposing any penalty under this Act, in respect of the case. Sec. 245 (H) (2) also empowers the Commission to withdraw the immunity so granted if the Commission is satisfied that in the process of the investigations the assessee has concealed any material particulars vital in relation to this case or that false evidence has been given by the assessee. In such a case, such person may be tried for the offence with respect to which the immunity was granted or any other offence in which he appears to be guilty in connection with the settlement. Such a person shall also become liable to pay penalty to which such person would have been liable, had such immunity not been granted.

(*vi*) ***Power to send the case back to Assessing Officer*** [Section 245 HA]

1. In case Settlement Commission is of the opinion that assessee is not cooperating in the proceedings, it may refer such case back to the Assessing Officer who shall dispose of the case as if no application for settlement was made.
2. The Assessing Officer shall be entitled to use all the material or reports of investigations produced before the Settlement Commission, as if they were produced before Assessing Officer.
3. For the purpose of calculating time limit to finalise the assessment proceeding before Assessing Officer the period commencing from the date on which application for settlement was made till the receipt of orders of referring back of the case shall be excluded.

(*vii*) **Order of Settlement Commission to be Conclusive** [Section 245 (I)]. The orders passed by the Commission shall be final and conclusive as regards the matters referred in the case cannot be re-opened in any proceedings.

(*viii*) **Recovery of Sums due under order of Settlement** [Section 245 (I)]. If any payment as provided under settlement orders is not forthcoming the Assessing Officer having jurisdiction over the defaulting person may use the powers conferred on him under chapter XVII regarding recovery of taxes. The Assessing Officer is also empowered to impose penalties for default in making payments.

(*ix*) **Bar on Subsequent Application for Settlement u/s 245(c)** (Section 245K). Under section 245 K if a person has applied to the Settlement Commission for settlement of his case and under the settlement order, penalty is imposed on the applicant for the concealment of some particulars of his income, such a person shall be debarred from applying for a settlement in relation to any other matters.

This section shall also debar a person from applying to the Commission, if under the Settlement order such person is convicted of an offence under chapter XXII of Income-tax Act.

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(*x*) **Proceeding to be Judicial** (Section 245 L). Any proceedings under this chapter before the Settlement Commission shall be deemed to be judicial proceedings.

RULES

(*xi*) **Form of Application for Settlement of a Case** (Rule 44 C). An application for settlement of a case shall be made is quintuplicate in Form No. 34 B.

(*xii*) **By whom to be Signed** (Rule 44 C). The application form and the form of verification shall be signed by:

(*a*) in case of individual by the individual himself;

(*b*) in case of H.U.F.—by the karta;

(*c*) in case of a company—by its managing director;

(*d*) in case of firm—by its managing partner;

(*e*) in case of local authority—by its principal officer;

(*f*) in case of any other association —by any member of the association, or by principal officer; and

(*g*) in case of any other person—by that person or some person competent to act on his behalf.

(*xii*) **Form to be accompanied by Fee** (Rule 44 C). Every application in connection with the settlement of case must be accompanied by a fee of Rs. 500 (Five hundred) only.

QUESTIONS

1. Write a brief essay on working of Settlement Commission.
2. What is the procedure for setting case through Settlement Commission ?
3. How is a Settlement Commission set up ? What are its powers ?

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6 APPEALS AND REVISIONS

Judicial authorities—Jurisdiction—Appeals—Appealable order—Appellate Tribunal, procedure in appeal—Appeal to High Court and Supreme Court—Revisions—Questions.

Income-tax Act, 1961, provides a remedial measure to an aggrieved assessee in the form of appeal against the orders issued by different Income-tax authorities.

AUTHORITIES

The judicial set up as provided in the Act is like this:

1. **Deputy Commissioner (Appeals).** It is the primary authority to whom an appeal at first instance can be made. The D.C. (A) shall have powers—

(*i*) to confirm, reduce, enhance or annul the assessment;

(*ii*) to set aside and refer the case back to the Income-tax Officer for making a fresh assessment in accordance with his directions and after making such further enquiry as may be necessary;

(*iii*) to confirm, cancel, enhance or reduce the penalty imposed;

(*iv*) in other cases to pass such orders in the appeal as he thinks fit.

The Deputy Commissioner (Appeals) has been given wide powers in disposing of an appeal he may consider fit and decide any matter arising out of the proceedings in which the order appealed against was passed notwithstanding that such matter was not raised before him by appellant.

Jurisdiction of Deputy Commissioner [(Appeals) Section 122]

Deputy Commissioners (Appeals) shall perform their functions in respect of such areas or of such persons or classes of persons or of such incomes or classes of incomes as the board may direct.

When any directions issued have assigned to two or more Deputy Commissioners, the same areas or the same persons or classes of persons or the same incomes or classes of incomes, they shall perform their functions in accordance with any order which the Board may make for the distribution and allocation of the work to be performed.

2. **Commissioner of Income-tax (Appeals).** The Finance Act (2) 1977 introduced as new appellate authority, namely Commissioner of Income-tax (Appeals),

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with a view to remove the existing drawbacks. As per existing provisions any tax-payer aggrieved by an order of the Assessing Officer can appeal to the Deputy Commissioner (Appeals) even in the cases where the order is made by the Assessing Officer on the basis of directions issued by the Deputy Commissioner, that they should sit in judgment on orders passed by their senior and experienced officers. In certain cases appeal against the decisions or orders passed by Deputy Commissioner lies with Commissioner of Income-tax who is an administrative authority and an appellate authority. These drawbacks have been removed with the appointment of Commissioner (Appeals).

The appeals to Commissioner (Appeals) shall lie against following cases:

(*a*) against an order made by Deputy Commissioner (Income-tax);

(*b*) against the order made by Assessing Officer after taking the prior approval of Deputy Commissioner;

(*c*) against the order made on the basis of statutory directions given by Deputy Commissioner;

(*d*) against the assessments made in case of all foreign companies and domestic companies whose assessed income exceeds Rs. 5 lakhs; or

(*e*) any other cases, which the CBDT may direct.

Jurisdiction of Commissioners (Appeals) [Section 121 A]

Commissioners (Appeals) shall perform their functions in respect of such areas or of such persons or classes of persons or such income or classes of incomes as the Board may direct.

Where under any directions issued, the Board has assigned to two or more Commissioners (Appeals), the same area, or the same persons or classes of persons or the same incomes or classes of income they shall perform their functions in accordance with any orders which the board may make for the distribution and allocation of the work to be performed.

The Finance Act, 1979 has amended Section 246. As per this amendment with effect from 1st June, 1979, appeals against all orders in the case of all categories of companies would lie to the Commissioner (Appeals) and that all such appeals pending before the Deputy Commissioner (Appeals) in the case of companies as on 1st June 1979 shall stand transferred to Commissioner (Appeals). The CBDT has been further empowered to transfer (by an order in writing) any appeal pending before Deputy Commissioner to the Commissioner (Appeals) where the CBDT finds it appropriate to do so having due regard to the nature of the case, the complexities involved and all other relevant considerations, in relation to the appeal or assessment.

3. **Appellate Tribunal.** If an assessee is not satisfied with an order passed by the Deputy Commissioner (Appeals), or Commissioner (Appeals) he is entitled under Section 253 to file an appeal to higher authority known as the Appellate Tribunal.

The Appellate Tribunal is the final authority on question of fact. Unlike Deputy Commissioner (Appeals) the Appellate Tribunal is not an Income-tax authority but it is a final fact-finding authority. The decision of Appellate Tribunal, on a question of fact, cannot be disturbed and it can be revised only where there is no evidence to support it or where the finding is perverse.

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Section 254, sub-sections (1), (2), (3), and (4) contain the provisions regarding:

(*i*) passing of an order in the appeal,

(*ii*) rectification of mistakes apparent from the record,

(*iii*) sending the copies of the order to the assessee, and

(*iv*) finality of the orders regarding question of the facts passed by the Appellate Tribunal.

4. **Reference to High Court and Supreme Court.** Any of the parties (assessee or Income-tax Department) aggrieved by an order of the Tribunal may require it to be referred to High Court, if any question of law is involved. On reference, High Court will give its decision regarding the question of law involved in the order passed by Tribunal.

Any party dissatisfied with the decision of High Court has the right to file an appeal to the Supreme Court, if the High Court certifies the case to be fit one for such appeal.

APPEALS

1. *Appeal to the Deputy Commissioner* (Appeals)

An appeal lies to the Deputy Commissioner (Appeals) against certain orders of the Income-tax Officer which have been expressly specified in Section 245 of the Income-tax Act. This section gives the right of appeal only to the tax-payer and not to the department.

The department cannot appeal against any order of the Assessing Officer to the Deputy Commissioner (Appeals). *Motor Union Ins. Co. Ltd.* vs. *C.I.T. 1945 I.T.R. 272.*

Appealable Orders [Section 246 (1)]

1. It proves that if the assessee feels aggrieved against any order of the Assessing Officer, subject to provisions of Section 246 (2), he can file an appeal to the Deputy Commissioner. The assessee may file an appeal against the following orders:

(*a*) (*i*) an order against the assessee where the assessee denies his liability to be assessed under the Act.

(*ii*) an order imposing a fine for alleged failure to attend in response to summons or to give evidence or produce books of accounts or other documents.

(*iii*) an order of assessment made under Section 143 (3) or Section 144 where the assessee objects to the amount of income assessed or the amount of tax determined, or to the amount of loss computed or to the status under which he is assessed.

(*b*) an order of assessment, re-assessment or re-computation under Section 147 or Section 150.

(*c*) an order of rectification under Section 154 or Section 155 enhancing the assessment or reducing the refund.

(*d*) an order under Section 163 treating the assessee as the agent of a non-resident.

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(*e*) an order under Section 170 (2) or 173 (3) making the assessee liable in respect of his predecessor's tax.

(*f*) an order under Section 171 on the question of the partition of a Hindu undivided family.

(*g*) an order under Section 185 (1) (*b*) or 185 (2) or 185 (3) or 185 (5) refusing to register a firm in respect of any assessment for the assessment year commencing on or before 1.4.92.

(*h*) an order under Section 186 (1) or Section 186 (2) cancelling the registration of a firm in respect of any assessment for the assessment year commencing on or before 1.4.92.

(*i*) an order under Section 201 under which a person is treated as assessee in default for his failure to deduct Income-tax at source or to pay it to the government.

(*j*) an order u/s 216 relating to the interest payable by assessee for wrongful deferment of the payments of advance tax or for under-payment of advance tax in the first three instalments.

(*k*) an order u/s 237.

(*l*) (*i*) against an order imposing penalties for default in paying tax on self-assessment u/s 221, for default in payment of tax u/s 271, for failure to furnish informations and particulars regarding securities etc. u/s 271, for failure to file a return u/s 139 (1), or 148 and for failure to comply with notice under Section 142 (1) or 143 (2).

(*ii*) an order imposing penalty under Section 272 or 272 B for failure to give notice of discontinuance or under Section 273 for false estimate or non-payment of advance tax.

(*m*) any partner may file an appeal against an order of the Assessing Officer regarding the computation of total income or loss of the firm or its apportionment thereof.

(*n*) any person who has paid and deducted tax at source in respect of any sum other than interest u/s 195 and who denies his liability to do so, may appeal to the Deputy Commissioner (Appeals).

2. Appeal to the Commissioner (Appeals) [Section 246 (2)]

Any assessee aggrieved by any of the following orders (which are made before or after the appointed day) may appeal to the Commissioner (Appeals) against such order:

(*a*) any order specified in points given above under the appeals to Deputy Commissioner (Appeals) where such order is made by Deputy Commissioner in exercise of the powers or functions conferred on or assigned to him under Section 120 or Section 124;

(*b*) any order u/s 104 as it stood before 1-4-88 in respect of assessment for the assessment year commencing on the 1st day of April 1987 or any earlier assessment year;

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(*c*) an order of assessment passed under section 143 (3) or 144, on the basis of directions issued by the Deputy Commissioner under section 144 A;

(*d*) an order made by Deputy Commissioner u/s 154;

(*e*) an order imposing a penalty under Section 271 (1B), where such penalty has been imposed with the prior approval of the Deputy Commissioner;

(*f*) an order made by Deputy Commissioner imposing a penalty under Section 272 A; or 272 AA; or

(*g*) an order made by an Assessing Officer in cases which the Board may direct.

Form of Appeal and Time Limit

The appeal shall be presented in the prescribed form and verified in the prescribed manner, within 30 days of the following dates, *i.e.*

(*a*) date of the service of the relevant notice of demand—provided that where an application has been made under Section 146 for re-opening of an assessment, the period from the date on which the application is made to the date on which the order on the application is served on the assessee shall be included, or

(*b*) date on which tax is deducted u/s 195 (1) relating to deduction of tax from payments to non-residents, or

(*c*) in any other case, the date on which intimation of the order against which appeal is preferred.

The D.C. (A) or Commissioner (Appeals) may admit an appeal after the expiry of the said 30 days if they are satisfied that the appellant had sufficient cause for not presenting it within period.

Pre-requisites for Appeal

No appeal shall be admitted unless at the time of filing of the appeal—

(*a*) where a return has been filed by the assessee, the assessee has paid the tax due on the income returned by him; or

(*b*) where the return has not been filed by the assessee, the assessee has paid an amount equal to the amount of advance tax which was payable by him.

Provided that, on an application made by the appellant in this behalf, the Deputy Commissioner (Appeals) may, for reason to be recorded in writing, exempt him from the operation of these provisions.

Procedure in Appeal [Sec. 250]

1. Under Section 250 (1), the D.C. (A) and Commissioner (Appeals) shall fix a day and place for the hearing of the appeal and shall give notice of the same to the appellant and to the I.T.O. against whose order the appeal is preferred.

2. The following shall have the right to be heard at the hearing of the appeal—

(*a*) the appellant either in person or by an authorised representative;

(*b*) Assessing Officer, either in person or by a representative [Sec. 250 (2)].

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3. The D.C. (A) or the Commissioner (Appeals) shall have the power to adjourn the hearing of the appeal from time to time. [Sec. 250 (3)].

4. The D.C. (A) or the Commissioner (Appeals), may before disposing off any appeal, make such further inquiries as they think fit or may direct the Assessing Officer to make further enquiry and report the result of the same. [Sec. 250 (4)].

5. The D.C. (A) or as the case may be Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal, not specified in the grounds of appeal, if the Deputy Commissioner (Appeals) or the Commissioner (Appeals) is satisfied that omission of that ground from the form of appeal was not wilful or unreasonable. [Sec. 250 (5)].

6. The order of the Deputy Commissioner (Appeals) or the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, decision thereon and the reason for the decision. [Sec. 250 (6)].

7. On the disposal of the appeal, the orders passed by them shall be passed on the assessee as well as to the Commissioner. [Sec. 250 (7)].

Powers of Deputy Commissioner (Appeals) or Commissioner (Appeals) [Section 251]

In disposing of the appeal, the D.C. (A) or the Commissioner (Appeals) as the case may be, has following powers:

(*i*) to confirm, reduce, enhance or annual the assessment;

(*ii*) to set aside the assessment and refer the case back to the Assessing Officer for making a fresh assessment in accordance with his directions and after making such further inquiries as he may consider necessary, and the Assessing Officer shall thereupon proceed to make such fresh assessment and determine, where necessary, the amount of tax payable on the basis of such fresh assessment;

(*iii*) to confirm, cancel, enhance or reduce the penalty imposed; and

(*iv*) in other cases to pass such orders in the appeal as he thinks fit.

The D.C. (A) or Commissioner (Appeals), as the case may be, will not pass any order enhancing the tax liability or a penalty or reducing the amount of refund without giving a reasonable opportunity to the appellant of being heard. He may pass orders on matters which may not have been referred to him.

Explanation. In disposing of an appeal, the D.C. (A) or, as the case may be, the Commissioner (Appeals) may consider and decide any matter arising out of the proceedings in which the order appealed against was passed, even if such matter was not raised before the D.C. (A) by the appellant (Sec. 251).

3. Appeal to appellate Tribunal

Constitution of Tribunal (Section 252). The Tribunal shall be constituted by the Central Government and shall consist of as many judicial and accountant members as it thinks fit. It shall discharge such functions and exercise such powers as are conferred on the Appellate Tribunal by the Act.

The judicial member shall be a person:

(*a*) who has held a civil judicial post for at least ten years, or

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(*b*) who has been a member of Central Legal Service (not below grade I) or any equivalent or higher post of at least three years, or

(*c*) who has been a practising lawyer for at least 10 years.

The period of service as advocate and the period of service on a civil judicial post may be aggregated for purposes of counting the experience of ten years.

The accountant member must be either (*a*) a Chartered Accountant who has been in practice of accountancy under the Chartered Accountants Act, 1949, for the last ten years; or (*b*) Commissioner of Income-tax who has served as such for at least three years; or on any equivalent or higher post, (*c*) a registered accountant under any law in force doing the practice of accountancy for the last 10 years either as registered accountant or partly as registered and partly as Chartered Accountant.

Ordinarily a judicial member of Appellate Tribunal shall be appointed as its President by the Central Government. The Central Government may appoint one or more members of the Tribunal to be the Vice-Presidents and the Vice-Presidents shall excercise such powers and perform such functions of the Presidents as may be delegated to them by the President by a general or special order in writing, Government has been empowered to appoint a senior Vice-President of the Tribunal as and where required.

Appealable Orders [Section 253]

The following matters may be referred to the Appellate Tribunal on an appeal by the assessee:

(*a*) an order passed by Deputy Commissioner (Appeals) or Commissioner (Appeals) relating to:

(*i*) rectification of mistake u/s 154; or

(*ii*) decision given on an appeal u/s 250; or

(*iii*) order of penalty u/s 271, or 271 A or 272 A; or

(*b*) an order passed by Commissioner u/s 263 under revisions; or

(*c*) an order passed by a Chief Commissioner or a Director General or a Director u/s 272 A.

The Assessing Officer can file an appeal on directions from Commissioner to the Appellate Tribunal only when the Deputy Commissioner (Appeals) decides a point against the authorities in an appeal or in an order under Section 159. The appeal can be filed under this section within 30 days only.

Form of Appeal and time of Appeal [Section 253 (6)]

The Appeal to the appellate Tribunal whether by assessee or by Assessing Officer must be filed within 60 days of the date on which the order against which appeal is being preferred, was communicated either to the assessee or to the Assessing Officer.

The appeal must be accompanied by a fee of Rs. 250 where the total income of the assessee as computed by the Assessing Officer is up to Rs. 100,000 and if such total income is more than Rs. 100,000 it is Rs. 1,500 if the appeal is filed by the

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assessee. No fee is to be paid in case the reference application is preferred by the Department.

Powers of the Appellate Tribunal [Section 254]

The Tribunal has the power to allow the appellant to withdraw an appeal.

Appellate Tribunal is not a Court but enjoys all the powers which any appellate Court enjoys under Code of Civil Procedure. *[Seshadri* vs. *I.T.O. 25 I.T.R. 400 & C.I.T.* vs. *Hazariwal Nagji 49 I.T.R. 1168].*

Section 254 (1) empowers the Appellate Tribunal to pass such orders, of course after giving both the parties to the appeal an opportunity of being heard, which it thinks just in relation to the matters that arise in the appeal. *[C.T.T.* vs. *Manick Sons 74 I.T.R. I. (S.C.)]*

It has been held in a number of cases that the Appellate Tribunal has a power to issue any type of order which it thinks desirable in the relevant case but at the same time it cannot sit on judgment on a matter which was not referred to the Tribunal for its decision and also cannot give a finding in a question which is not in dispute and which does not form the subject-matter of the appeal before it. *[Pokhraj Hirachand* vs. *C.I.T. 49 (I.T.R.) 293].*

In a case Omar Salar Mohammad *v.* C.I.T., the Supreme Court has observed that while giving its judgement, the Tribunal must consider every fact for and against the assessee with due care and not act on conjectures or irrelevant considerations.

Under Section 254 (2) with a view to rectifying any mistake apparent from the record the Appellate Tribunal may, at any time within 4 years of the date of the orders, amend any order passed by it and shall make such amendment if the mistake is brought to its notice by the assessee or the Assessing Officer.

In a case where any amendment results into enhancement of the assessment or reducing the refund if any, or otherwise increasing the liability of the assessee, the assessee must be served with a notice by the Appellate Tribunal of its intention to do so and must allow the assessee a reasonable opportunity of being heard.

Procedure in Appeal [Section 255]

The Appellate Tribunal shall form itself in benches constituted by its President and every Bench shall exercise the powers and discharge the function of Appellate Tribunal. The Bench shall consist of one judicial member and one accountant member.

The Tribunal shall have powers to regulate its proceedings in its own manner. The Tribunal shall for the purpose of discharging the functions have all the powers conferred upon different Income-tax authorities under Section 131. The proceedings before the Appellate Tribunal shall be deemed to be judicial proceedings for Section 196 of I.P.C.

In case of disagreement on any issue in appeal between the members of the Bench, the matter has to be referred by the President to one or more members of the Tribunal and the matter will be decided by a majority of the members who hear the case including the members who heard it.

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In case of appeal by an assessee whose tax liability does not exceed Rs. 1,00,000 (as computed by Assessing Officer), the President or any other member of the Tribunal may dispose it off sitting single.

4. *Reference to High Court* [Sections 256 to 260]

Section 256 of the act provides that the assessee or Commissioner may within 60 days of the order of the Appellate Tribunal, require the Appellate Tribunal to refer to the High Court of the State concerned any question of law arising out of such order. Such a reference shall be made on an application by the assessee or by the Commissioner and shall be accompanied by a fee of Rs. 200 if it is preferred by the assessee and irrespective of the number of questions of law specified in the application.

The Tribunal shall, within 120 days of the receipt of such application draw up a statement of the case and refer the case to High Court or refuse to refer the case on the grounds that no question of law is involved. In such a case, the assessee or the Commissioner, as the case may be, within 6 months of the date on which he is served with notice of such refusal, apply directly to the High Court. If the High Court is not satisfied with the decision of the Appellate Tribunal, it may require the Appellate Tribunal to state the case and refer it and on receipt of such requisition the Appellate Tribunal shall do so.

In any case where a proper application to the Tribunal is made to state the case and refer it to the High Court, it is obligatory on the part of the tribunal to send the reference to the High Court if a question of law does arise out of the Tribunal's appellate order *[Banarsi Dass & Co., Ltd.* vs. *I.T. Tribunal 35 I.T.R. 624].*

Rule 41 requires the reference application to be signed either by the assessee or by his authorised representative and the application should state the question of law which arises out of the order of the Tribunal and which the assessee desires to be referred to the High Court. While referring the question to the High Court, the Tribunal may or may not accept the questions framed by the assessee and it may reformulate the question in its own language.

In case his reference application is rejected on the ground that no question of a law arises, the applicant can withdraw his application and in such a case he is allowed the refund of the fees also. But no refund will be allowed if his application was rejected being time-barred. In case the assessee opts to withdraw his application and thus gets the refund of the fees, he cannot thereafter make an application to the High Court u/s 256 (2).

In case the Tribunal has found that no question of law arises out of its order and aggrieved party has referred its case to the High Court u/s 256 (2), it is for the Court to determine what question or questions of law arise out of the appellate order of the Tribunal. Even when the Court has sent a requisition to the Tribunal to state a case and refer it to the Court, the Court's requisition should indicate the question or questions of law which according to the High Court arise out of the Tribunal's appellate order.

At the end it can be said that all questions of facts regarding assessee's income are for Tribunal to decide and the Court cannot go beyond the Tribunal's finding of fact. A reference to the Court can only be preferred on a question of law.

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In case the assessee dies during the pendency of his reference proceedings, the proceedings may be continued by or against his legal representatives. *[Maharaja of Darbhanga vs. C.I.T. 283].*

The case referred to high Court shall be heard by a Bench of at least two or more of the High Court judges, and it shall always be decided in accordance with the opinion of majority of the judges.

Under Section 260, the High Court, upon hearing in any such case shall decide the questions of law and shall deliver its judgement stating the grounds on which such decision is based. A copy of the judgement shall be sent to the Appellate Tribunal to enable it to pass necessary order for the disposal of the case in accordance with the decision.

5. *Appeal to Supreme Court* [Section 261]

Any party dissatisfied with the decision of the High Court, has the right to file an appeal against such decision to the Supreme Court. The appeal shall be disposed off by the Supreme Court in the same manner as it adopts in case of other appeals from the decrees of High Courts. When the Supreme Court varies its judgement from that of High Court, the Tribunal shall pass such orders as are necessary to dispose off the case in the light of the judgement of the Supreme Court.

An appeal shall lie to the Supreme Court from any judgement of the high Court delivered on a reference made u/s 256 by the Tribunal to the High Court. This appeal can be filed only if the High Court certifies the case to be a fit case for appeal to the Supreme Court. In case the High Court finds that the case is not worth referring to the Supreme Court and so refuses to certify the case to be a fit one for appeal to the Supreme Court, an application may be made to the Supreme Court under Article 136 of the constitution for special leave to appeal.

Normally, the High Court is supposed to certify the case as a fit one for appeal and grant leave to appeal to the Supreme Court if a substantial question of law is involved in that case and the same is likely to occur in successive years and otherwise also the question is of great public and private importance.

Direction Reference of a Case to the Supreme Court [Section 257]

If any application made for reference, is on a point on which there are conflicting decisions of the different High Courts, the Appellate Tribunal may refer the matter through its President direct to the Supreme Court.

GENERAL PROVISIONS

Tax to be paid notwithstanding reference etc. [Section 265]

Notwithstanding that a reference has been made to the High Court or the Supreme Court, or an appeal has been referred to the Supreme Court, tax shall be payable in accordance with the assessment made in the case.

Execution of orders for costs awarded by the Supreme Court [Section 266]

On a petition made for the execution of orders of the Supreme Court, in respect of any costs awarded thereby, the High Court may transmit the order for execution to any Court subordinate to the High Court.

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Amendment of Assessment on appeal [Section 267]

In case any change is made or new assessment is made, as a result of appeal u/s 246 or 253, on the assessment of Association of Persons or Body of Individuals, the Deputy Commissioner (Appeals), Commissioner (Appeals) or the Appellate Tribunal may direct the Assessing Officer either to amend the assessment already made or to make the assessment afresh.

Exclusion of time taken for copy [Section 268]

In computing the period of limitation prescribed for an appeal, or an application under this Act, the day on which the order complained of was served and if, the assessee was not furnished with a copy of the order when the notice of the order was served upon him, the time required for obtaining a company of such order shall be excluded.

REVISION

Revision of a Best Judgement Assessment [Section 146]

The assessee may, under prescribed circumstances, make an application to the Assessing Officer against his orders issued under Section 144 of the Act making Best Judgement Assessment for not complying with the notices issued under Section 139 (2) or 142 (1) or 143 (2) for revision of such orders. The prescribed grounds are:

(*i*) That he was prevented by sufficient cause from filing the return under Section 139 (2), or

(*ii*) That he did not have a reasonable opportunity to comply or was prevented by sufficient cause from complying with the terms of any notice served either under Section 142 (1) or under Section 143 (2).

In case the Assessing Officer is satisfied with the contention of the assessee, he shall cancel the original Best Judgement Assessment and shall make a fresh regular assessment.

Revision by Commissioner

(*i*) **Revision of orders Prejudicial to Revenue.** Section 263 of the Act, gives powers to Chief Commissioner or Commissioner to review any orders passed by Assessing Officer and to pass such orders thereon as the circumstances of the case justify. While passing such orders he may enhance, cancel or modify an assessment or he may order a fresh assessment. The assessee has to be provided an opportunity of being heard in this case.

No order shall be made under this section after the expiry of two years from the end of financial year in which the order sought to be revised was passed.

Explanation. For the removal of doubts, it is hereby declared that, for the purposes of this sub-section—

(*a*) an order passed by the Assessing Officer shall include—

(*i*) an order of assessment made by the Assistant Commissioner or the Assessing Officer on the basis of the directions issued by the Deputy Commissioner under section 144 A;

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(*ii*) an order made by the Deputy Commissioner in exercise of the powers or in the performance of the functions of an Assessing Officer conferred on, or assigned to him under the orders or directions issued by the Board or by the Chief Commissioner or Director General or Commissioner authorised by the Board in this behalf under section 120;

(*b*) "record" includes all records relating to any proceeding under this Act available at the time of examination by the Commissioner;

(*c*) where any order referred to in this sub-section and passed by the Assessing Officer had been the subject mater of any appeal, the powers of the Commissioner under this sub-section shall extend to such matters as had not been considered and decided in such appeal.

But u/s 263 (3) an order of revision may be passed at any time in the case of an order which has been passed in the light of any finding or direction contained in an order of the Appellate Tribunal, the High Court or the Supreme Court.

Under this section, the Commissioner has been armed with the power of revising an order of the Assessing Officer primarily because the department has no right of appeal to the Deputy Commissioner (Appeals) against the orders passed by the Assessing Officer.

The important point to be noted in this connection is that the commissioner must have gathered necessary information to show that the assessment order passed by the Assessing Officer has been erroneously passed and is prejudicial to the revenue as well.

The spirit of Section 264 is that the Commissioner may be given such powers whereby he may be able to revise such orders which are prejudicial to the assessee and thus this section empowers him to exercise his powers in favour of the assessee. It has been held in a case that it is the power coupled with a duty to exercise it in the interest of justice to the assessee. *[Hirday Narain* vs. *I.T.O. 78 I.T.R. 26 (S.C.)].*

The Commissioner can exercise his revisional power only if the original order is not appealable or if appealable, the assessee has either waived his right of appeal already or the appeal has become time-barred.

(*ii*) **Revision of other orders.** Under the provisions of section 264 in case of any order, other than that to which Section 263 applies, passed by authority subordinate to him, the Commissioner may either of his own motion or on application by the assessee for revision, call for the record of any proceedings, under the Act in which any such order has been passed and make such inquiries and orders thereon as he thinks fit. These orders cannot be prejudicial to the assessee.

In this case the revision proceedings can be started by the Commissioner of his own motion within one year of the passing of the order sought to be revised. If the assessee wants revisions of any order, the application accompanied by a fee of Rs. 25 only must be made within one year of the date on which the order in question was communicated to him or the date on which he otherwise comes to know of it, whichever is earlier.

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The Commissioner shall not revise any order under this section in the following circumstances:

(*a*) Where an appeal against the order lies to the Deputy Commissioner (Appeals) or to the Appellate Tribunal or it has not been made and the time for its making has not expired or in the case of an appeal to the Tribunal, the assessee has not waived his right of appeal; or

(*b*) Where the order is pending on an appeal before the Deputy Commissioner (Appeals); or

(*c*) Where an appeals has been made to Appellate Tribunal against the order.

An appeal can be made by assessee to the Tribunal against the order u/s 263 but no appeal can be made against the order under Section 264.

QUESTIONS

1. Describe the procedure of an appeal to the Deputy Commissioner (Appeals). Give various orders against which the appeal can be preferred.
2. Describe the procedure of constitution of appellate Tribunal. Give the procedure for filing an appeal to the Appellate Tribunal.
3. (*a*) Write a short note on Reference of a case to High Court and Supreme Court by an assessee.

   (*b*) Describe the various cases in which the assessment can be revised by the Commissioner.

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7 PENALTIES AND PROSECUTION

Various types of Penalties—Failure to file return—Concealment of income—Firm—Failure to pay advance tax—Powers to waive penalty—Stay or compounding—Procedure for levying penalty—Prosecutions—Offences of individual, H.U.F., Firm and Companies—Questions.

"The tax statutes should provide a broad range of monetary penalties which can be assessed by the administrative authorities and imprisonments which can be imposed by the courts."[1]

With the increase in the number of tax-payers, it is essential that the tax administration must be honest, consistent and expeditious, in case it is desired that the tax laws are observed voluntarily. Every tax-payer tries to minimise his tax liability and if willful evasion is allowed to succeed, it will not only lead to revenue loss but will bring general disrespect for the law. As such it becomes necessary that statute should provide for appropriate penalties and prosecutions to discourage such tendency. However, honest tax-payers, who commit mistakes due to ignorance should be let off lightly.

PENALTIES

Under Income-tax Act penalties are imposed either by the departmental authorities in certain cases or are imposed by the court for certain Income-tax offences.

The power to impose a penalty is given to Assessing Officer and the Commissioner. In the case of *Bansi Lal* vs. *C.I.T. 83 I.T.R. 750* it was held that the right to impose penalty by I.T.O. does not come to an end when an appeal in filed against the assessment made by him although in certain cases he has to obtain the prior approval of the Deputy Commissioner. The above-mentioned income-tax authorities are empowered to impose penalties for default in the course of proceedings going on before them. Penalties are imposable on the assessee by the D.C. (A) in an appeal filed by the assessees against the order of Assessing Officer [*Kamalpat Moti Lal* vs. *C.I.T. 45 I.T.R. 266 (S.C.)* and *Modern Works* vs. *C.I.T. 93 I.T.R. 164]*. The Assessing Officer cannot impose a penalty on the concealed income detected by D.C. (A) in the course of appeal against the assessment completed by the Assessing Officer (*C.I.T.* vs. *Shadi Ram Balmukund 84 I.T.R. 183).*

1. William J. Shultz and C. Lowell Harriss, *American Public Finance, 1965, p. 194.*

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It is also possible that the D.C. (A) may allow an appeal of the assessee against the orders of penalty of Assessing Officer, and may himself impose a fresh penalty (*Ghulam Hussain* vs. *C.I.T. 23 I.T.R. 309).*

The Income-tax Act, 1961 prescribes various types of penalties in the even of defaults under the Act. These are:

1. **For Failure to pay tax** [Section 221 (1)]. If the assessee, on whom notice of demand has been served, fails to pay the specified amount of tax, he shall be liable to a penalty which the Assessing Officer, may, from time to time, direct, however the total amount of penalty shall not exceed the amount of tax due.

2. **For Failure to pay tax on Self-Assessment** (Section 140 A). If the assessee fails to pay the amount of tax on the basis of self-assessment he will be liable to a penalty to be imposed @ 2% of the tax due on self-assessment of each month of default.

In both the cases above, the assessee must be given a reasonable opportunity of being heard.

3. **For Non-Compliance with Notice under Section 142 (1) or 143 (2)** [Section 271 (1)(b)]. If the A.O., D.C. (A) or Commissioner (Appeals), in the course of any proceedings under this Act, is satisfied that any person has without any reasonable cause failed to comply with a notice u/s 142 (1) or 143 (2) or fails to comply with the directions issued u/s 142 (2A) (auditing of accounts by Chartered Accountants) the above mentioned authorities may direct that such person shall pay by way of penalty equal to a sum which shall not be less than Rs. 1,000 of each failure but which shall not exceed Rs. 25,000 for each failure. The penalty shall be in addition to any tax payable by him in this regard.

4. **For Concealment of Income** [Section 271 (1) (c)]. Where any person has concealed the particulars of his income or has furnished inaccurate particulars of such income, he will be liable to a penalty. The minimum penalty leviable for concealment has been fixed at not less than 100% but not exceeding 300% of the amount of tax *sought to be evaded* by reason of concealment of income.

It has been held in *C.I.T.* vs. *Shadiram Balmukand* in clear terms that the Assessing Officer cannot impose a penalty in respect of the additional concealed income discovered by the Deputy Commissioner (Appeals) in the course of an appeal against the assessment.

In case unexplained cash credits are added to the assessee's income, no penalty can be imposed for concealment in respect of such income unless such cash credits constitute income in the relevant year [*C.I.T.* vs. *Bhuramal Manik Chand*].

5. **Registered Firm** [Sec. 271 (2)]. In case penalty is levied on a registered firm or unregistered firm assessed as registered firm u/s 183 (b), then the penalty imposable u/s 271 (1) shall be equal to the same amount as would be imposable as if that firm was an unregistered firm.

6. **For Wrong Distribution of Profit by Registered Firms** [Section 271 (4)]. If the profits of a registered firm are distributed in such a way that the share of a partner is shown below the real amount and if such a partner returns his income below the real amount, he shall in addition to tax if any payable by him, be liable to pay a penalty of 150% of the difference between tax on partner's income assessed and tax on income as returned. In such a case no refund or other adjustment shall be claimable by any other partner by reason of such direction.

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7. **For Failure to keep, maintain or retain books of account, documents, etc.** [Section 271 A]. If any person fails to keep and maintain books or documents as required by Section 44 AA, he will be liable to a penalty which may be equal to a sum which shall not be less than Rs. 2,000 but which may extend to Rs. 1,00,000 (one lakh).

8. **Failure to get accounts audited** [Sec. 271 B]. If any person fails to get his accounts audited in respect of any previous year or years or furnish the said report along with the return of his income filed u/s 139 (1) or 142 (1) (*i*), the Assessing Officer may direct that such person shall pay a penalty equal to one-half ($^1/_2$) per cent of the total sales, turnover of gross receipts in business or of the gross receipts in profession or a sum of one hundred thousand rupees, whichever is less.

9. **For failure to subscribe to the eligible issue of Capital** [Section 271 BB]. In case any mutual fund or U.T.I. fail to subscribe any amount of subscriptions to the units issued under any scheme referred to in section 88 A of the Act, to the eligible issue within the period of 6 months, it may be directed by Deputy Commissioner of Income-tax to pay, by way of penalty, a sum equal to 20% of such amount.

10. **Penalty for failure to deduct tax at source** [Sec. 271 C]. If any person fails to deduct the whole or any part of the tax as required by or under the provisions of the Act, or fails to pay whole or any part of tax deducted at source ; he shall be liable to pay a penalty which shall be a sum equal to the amount of the tax which he failed to deduct or pay as required.

11. **Penalty for Failure to comply with the provisions regarding accepting of loans etc.** (Sec. 271 D). If a person takes or accepts any loan or deposit exceeding Rs. 20,000 except through crossed payee's cheque or draft, he shall be liable to pay penalty which shall be a sum equal to the amount of the loan or deposit so taken or accepted.

12. **Penalty for Failure to comply with the provisions of Sec. 269 T** (Sec. 271 E). If a person repays any deposit exceeding Rs. 20,000 otherwise than by crossed cheque or draft, he shall be liable to pay penalty which shall be a sum equal to the amount of the deposit so repaid.

Any penalty to be levied u/s 271 C, 271 D and 271 E shall be levied only by Deputy Commissioner [*Inserted by the finance Act, 1990*].

13. **Penalty for non filing of return** [Section 271 F]

In case a person whose is required to furnish a return of his income u/s 139(1) on or before the due date he shall be liable to a penalty of Rs. 500.

14. **Penalty on failure to answer questions, or sign statements, etc.** [272 A (1)]. In case an assessee is found guilty of any of the following offences, he shall pay, by way of penalty, a sum which shall not be less than Rs. 500 but which may extend to Rs. 10,000 for each such default:

(*a*) A person who is legally bound to state the truth regarding subject to his assessment, refuses to answer any question put to him by an income-tax authority; or

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(*b*) A person who is legally required to sign any statement made by him, refuses to sign; or

(*c*) A person to whom summons are issued to produce books of account or other evidence or to attend personally to give evidence, at certain place and time, fails to do so;

(*d*) A person who fails to comply with the provisions of section 139 A regarding permanent account numbers.

15. **Failure to comply with certain notices or to furnish certain returns, statements or to allow inspections** [Section 272 A (2)]. In case a person fails—

(*a*) to comply with notice issued u/s 94 (6) of the Act regarding information about securities held by assessee;

(*b*) to give a notice of discontinuance of business required u/s 176 (3);

(*c*) to furnish in due time following returns, or statements—

(*i*) u/s 133—statement regarding information called for by assessing Officer;

(*ii*) u/s 206—return regarding tax deducted at source;

(*iii*) u/s 206 A—return regarding person from whom tax has not been deducted at source out of interest paid to them;

(*iv*) u/s 206 B—return regarding person to whom dividend has been paid without deducting tax at source;

(*v*) u/s 206 C—return regarding deduction of tax at source in case of profits from alcoholic liquor etc.

(*vi*) u/s 285 B—statements by producers of films.

(*d*) to allow inspection of any register or to allow copy being taken of any of these registers;

(*e*) to furnish a return of income by a trust u/s 139 (4A);

(*f*) to deliver in due time a copy of the declaration received from assessee for not deducting the tax at source, u/s 197A;

(*g*) to furnish a certificate as required u/s 203 regarding tax deducted at source; or

(*h*) to deduct and pay tax as required u/s 226 (2)

he shall pay, by way of penalty ranging between Rs. 100 to Rs. 200 for every day of default.

In case of—

(*a*) an offence falling under (*f*) above, the penalty may be levied by the Chief Commissioner or the Commissioner;

(*b*) in all other offences it will not be levied by any authority below the rank of Deputy Commissioner [Section 272A (3)].

Provided that the amount of penalty for failures in relation to returns under sections 206 and 206 C shall not exceed the amount of tax deductible or collectible as the case may be.

16. **For Failure to comply with the provisions of Sec. 133 B.** The new Section 272 AA provides for penalty for failure to comply with the provisions of Section 133

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B regarding entry of income-tax authorities in any building etc. The penalty for noncompliance may extend upto Rs. 1,000. Before levying any penalty the assessee must be given an opportunity of being heard.

17. **For Failure to comply with provisions of Section 203 A** (Section 272 BB). If a person fails to comply with the provision of Section 203 A *i.e.* to apply for Tax deducted at Source Account number, the Assessing Officer shall impose a penalty which may be equal to Rs. 5,000; giving the assessee an opportunity of being heard.

Power to Reduce or Waive Penalty, etc. in Certain Cases (Sec. 273 A). The Income-tax Act has empowered the Chief Commissioner or the Commissioner to reduce or waive the penalty etc. in certain cases. Sec. 273 (1) says that notwithstanding anything contained in this Act, the Chief Commissioner or the Commissioner, may, at his discretion, whether on his own motion or otherwise, reduce or waive the penalty in the following cases:

(*a*) The Chief Commissioner, or the Commissioner may reduce or waive the penalty leviable under sec. 271 (1) (*iii*) for assessee's failure to disclose all the facts and particulars of his income.

(*b*) The Chief Commissioner, or the Commissioner shall exercise power to reduce or waive the penalty only if he is satisfied that the assessee has disclosed all the facts of his income, before any detections made by the Assessing Officer, voluntarily and in good faith and he has made a true disclosure of all the relevant particulars.

The point to be noted in this connection is that the assessee must have co-operated in any inquiry relating to the assessment of his income and has either paid or made satisfactory arrangements for the payment of any tax or interest payable in consequence of an order passed under this Act.

Board's Permission [Sec. 273 A (2b)]. In the following cases, the Chief Commissioner, or the Commissioner has to seek Board's permission before any order to reduce or waive the penalty is made by him if the amount of income in respect of which the penalty is imposed or imposable or where such disclosure relates to more than one assessment year and then the aggregate amount of such income of those years, exceeds Rs. 5,00,000.

Stay or Compounding Proceedings [Sec. 273 A (4)]

Section 273A (4) empowers the Chief Commissioner or the Commissioner that he may, on an application made by the assessee in this behalf, and of course after recording his reasons for so doing, reduce or waive the amount of any penalty payable by the assessee under this Act or stay or compound any proceedings for the recovery of any such amount, if he is satisfied that—

(*i*) to do otherwise would cause genuine hardship to the assessee, having regard to the circumstances of his case.

(*ii*) the assessee has co-operated in any inquiry relating to the assessment or any proceeding for recovery of any amount due from him.

Section 273 A (5) says that every order made under this section shall be final and shall not be called into question by any court or any other authority.

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Regarding waiving or reducing the penalty u/s 273A, the Board of Direct Taxes in one of its circulars has stated the opinion of the Ministry of Law that the discretion to reduce or waive penalty can be exercised only in those cases where the return of the income was duly filed before the last day of the relevant assessment year.

Procedure for imposing penalty

According to the provisions of section 274, if any penalty of the aforesaid nature is to be imposed, the assessee must be provided with a reasonable opportunity of being heard. If no such opportunity is provided to the assessee, the penalty order will be invalid.

No order imposing a penalty, can be made without prior approval of Deputy Commissioner—

(*a*) where penalty exceeds Rs. 10,000 levied by I.T.O.

(*b*) where penalty exceeds Rs. 20,000 levied by Assistant Commissioner. [Section 274 (2)].

An Income-tax authority on making an order imposing a penalty, unless he himself is an Assessing Officer, shall forthwith send a copy of such order to the Assessing Officer. [274 (3)].

Time limits of commencement and completion of penalty proceedings (Section 275). This section prescribes time limits both for commencement and for completion of penalty proceedings. No order imposing a penalty under this chapter shall be passed—

(*a*) in a case where the relevant assessment or order is the subject-matter of an appeal to the D.C. (A) or the commissioner (Appeals) under Section 246 or an appeal to the Appellate Tribunal under Section 253 after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty been initiated, are completed or six months from the end of the month in which the order of the Deputy Commissioner (Appeals) or the Commissioner (Appeals) or as the case may be, the Appellate Tribunal is received by the Chief Commissioner or the Commissioner whichever period expires later.

Above-mentioned legal language can be expressed simply as below—

After the expiry of two years from the date of completion of the proceedings, in the course whereof the penalty proceedings were initiated, or six months from the end of the month in which the order of the Deputy Commissioner (Appeals), or the Appellate Tribunal is received by the Commissioner, which period expires later no order imposing a penalty can be passed—

(*b*) in any other case after the expiry of 2 years from the end of the financial year in which the proceedings, in the course of which action for imposition of penalty has been initiated, are completed.

While calculating the above periods of limitation the following period shall be excluded:

(*i*) The time taken in giving an opportunity to the assessee to be heard under Section 129;

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(*ii*) Any period during which the immunity granted under Section 145 H remained in force; and

(*iii*) Any period during which proceedings under this chapter for the levy of penalty are stayed by an order or injunction of any court.

Sl. No.	*Section*	*Offence*	*Penalty*
1.	221 (1)	Failure to pay tax	Maximun upto tax due
2.	234 A & B	Failure to pay tax on self assessment u/s 140A	2% of tax due for delay or each month or part thereof
3.	271 (1)(b)	Non compliance of notice served u/s 142(1) or 143(2) or 142(2A)	Rs. 1,000 to Rs. 25,000 for each failure
4.	271 (1)(C)	Concealment of income	100% to 300% of tax saught to be evaded.
5.	271 A	Failure to keep maintain or retain books of accounts u/s 44AA	Rs. 2,000 to Rs. 1,00,000
6.	271 B	Failure to get accounts audited	1/2% of total sales, turnover or gross receipts of business or gross receipts of profession, subject to maximum of Rs. 1,00,000
7.	271 BB	Failure by Mutual funds or UTI to invest in egilible issue	Penalty of an amount equal to 20% of such amount
8.	271 C	Failure to deduct tax at source	Penalty of a sum equal to amount of tax not deducted
9.	271 D	Accepting deposits exceeding Rs. 20,000 in cash u/s 269SS	Penalty equal to amount of deposit or loan accepted
10.	271 E	Payment of deposits or loan exceeding Rs. 20,000 in cash u/s 269T	Penalty equal to amount of deposit or loan repaid
11.	271 F	Non filing of return	Rs. 500
12.	272 A(1)	Failure to answer questions or sign statements	Rs. 500 to Rs. 10,000 for each such default
13.	272 A(2)	Failure to comply with notices served u/s 94(6), 176(3) or failure to submit statement or return u/s 133, 206, 206A, 206 206C or u/s 285B, u/s 139 (4A), u/s 197A, 203 u/s	Penalty of Rs. 100 to Rs. 200 per day of default
14.	272 AA	Failure to comply with provision of section 133B	Penalty for non-compliance is Rs. 1,000
15.	272 BB	Failure to comply with 203A-tax deduction account number	Penalty of Rs. 5,000
16.	158 BFA	Undisclosed income due to search & seizure under block assessment	Penalty equal to 100% of tax on such undisclosed income.

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PROSECUTIONS

There are some lapses on the part of the assessee which are punishable through the courts. Whenever Income-tax department feels that a particular person has committed a particular offence, a wrongful act or he is guilty of a crime, the department will initiate the proceedings before a magistrate. The proceedings, before the magistrate shall be heard under the Criminal Procedure Code and onus to prove the guilt before the magistrate shall fall upon the department. The assessee is considered to be an innocent person unless proved otherwise. Punishment given by the department is of monetary nature whereas for some specific offences punishment can be in the shape of imprisonment. But for that, the Income-tax authorities have to launch the proceedings in a court of law. The following are cases where the person commits offence under the Act, making the guilty persons liable to be punished by the court.

1. **For removing any Asset, Books of account, documents etc. found during search in contravention of order served under Section 132 (3).** Such a person shall be punishable with rigorous imprisonment which may extend upto 2 years and shall also be liable to fine. (Section 275 A).

2. **Removal, Concealment, transfer or delivery of property to avoid tax recovery** [Section 276]. When a person fraudulently removes, conceals, transfers or delivers an asset with the objective of thwarting recovery of tax, he shall be liable to rigorous imprisonment upto 2 years and with fine.

3. **Default on the part of Liquidator** [Section 276 (A)]. Under the provisions of Section 178 (1), a liquidator of a company is supposed to inform the Assessing Officer about his appointment as such within 30 days. Under Section 178 (3) he is required not to part with any assets or properties without the permission of the Commissioner. He is further supposed to set aside an amount equal to the amount of tax payable by the company (as intimated by the I.T.O.).

If the liquidator contravenes any of these provisions, he shall be punishable with rigorous imprisonment which may extend upto a maximum of 2 years. If there are no special reasons, the imprisonment shall not be less than 6 months.

4. **Failure to comply with provisions regarding transfer of immoveable property** [Section 276 AB]. When a person fails to comply with provisions u/s 269 UC, 269 UE and 269 UL, (covered under acquisition of immovable property) he shall be liable to a punishment of rigorous imprisonment upto 2 years and with fine. If there are no special reasons, the imprisonment shall not be less than 6 months.

5. **Failure to pay the tax deducted at source** [Section 276 B]. If a person fails to pay to the credit of the Central Government the tax deducted at source by him as required by or under the provision of this Act, he shall be punishable with rigorous imprisonment for a term which shall not be less than 3 months but which may extend to 7 years and with fine.

6. **Failure to pay the tax collected at source** [Section 276 (BB)]. If a person fails to pay to the credit of the Central Government, the tax collected by him as

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required under the provisions of Section 206 C, he shall be punishable with rigorous imprisonment for a term which shall not be less than three months but which may extend to seven years and with fine.

7. **Wilful attempt to evade Tax, Penalty, Interest etc.** [Section 276 C (1)]. If a person intentionally tries to evade any tax, penalty or interest, he shall be liable to a punishment of rigorous imprisonment of 6 months to 7 years and fine if the tax sought to be evaded exceeds Rs. 1,00,000 and 3 months to 3 years and fine if the amount of evasion is less than Rs. one lakh.

In case a person willfully attempts to evade the payment of tax, penalty or interest, he shall be punishable with rigorous imprisonment of a term from 3 months to 3 years and with fine [Section 276 C(2)]. The punishment of imprisonment is without prejudice to any penalty that may be imposable on him under any other provision of the Act.

Explanation: The term wilful attempt to evade any tax, penalty or interest etc. shall include in the following cases:

(*i*) The person concerned has in his possession or control any books of account or other documents (relevant to any proceedings under this Act) containing a false entry or statement.

(*ii*) He makes or causes to be made any false entry or statement in such books of account or other documents.

(*iii*) He wilfully omits or causes to be omitted any relevant entry or statement in such books of account or other documents.

(*iv*) He causes any other circumstance to exist which will have the effect of enabling such person to evade any tax, penalty or interest chargeable or imposable under this Act, or the payment thereof.

8. **Failure to furnish Return of Income.** (Section 276 CC). If a person wilfully or intentionally fails to furnish in due time the return of income which he is required to furnish u/s 139 (1) or 142 (1)(*i*) or 148, he shall be punishable:

(*i*) In a case where the amount of tax which would have been evaded if the failure had not been discovered, exceeds Rs. 1,00,000 with a rigorous imprisonment which shall not be less than 6 months but which may extend to 7 years and with fine;

(*ii*) in any other case, with imprisonment which shall not be less than 3 months but which may extend to 3 years and with fine.

It may be noted that person shall not be proceeded against under this section in the following cases:

(*i*) For any assessment year commencing prior to 1-4-1975.

(*ii*) For any assessment year commencing on or after 1-4-1975 if—

(*a*) the return is furnished by him before the expiry of the assessment year; or

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(*b*) the tax payable by him on the total income determined on regular assessment, as reduced by the advance tax paid, if any, and any tax deducted at source, does not exceed Rs. 3,000.

9. **Failure to furnish return of income in search cases u/s 158 BC** [Section 276 CCC]

In case a person willfully fails to furnish in due time, return of total income under a notice served u/s 158 BC, he shall be punishable with imprisonment for 3 months to 3 years and with fine.

10. **Failure to produce Accounts and documents** [Section 276 (D)]. If a person willfully fails to comply with the provisions of the notice served under Section 142 (1) regarding production of accounts, books or other documents, or willfully fails to comply with a direction issued to him under section 142 (2A) to get accounts audited by a Chartered Accountant, he shall be punishable with rigorous imprisonment which may extend upto one year or fine of Rs. 4 to Rs. 10 per day of default or with both.

11. **False Statement in Verification** (Section 277). A person making a false statement or delivering a false account or statement which he either knows or believes to be false or does not believe to be true, shall be punishable with rigorous imprisonment for 6 months to 7 years, if the amount of tax evaded would have been more than Rs. one lakh and 3 months to 3 years and fine in any other case.

12. **Abetment in False Return** (Section 278). If a person abets or induces in any manner another person to make and deliver a false account, statement or declaration relating to any income chargeable to tax or to commit an offence u/s 276 C (1), he shall be punishable with rigorous imprisonment for a minimum term of six months and a maximum of seven years, if the amount of tax evaded would have been more than Rs. 1,00,000 and 3 months to 3 years in any other case and with fine.

13. **Punishment of Second and Subsequent Offences** (Section 278 A). If a person convicted of an offence under Section 276 B, 278 C(1), 276 CC, 276 DD, 276 D, 276 E, 277 or 278 is again convicted for an offence under any of these provisions, he shall be punishable for second and every subsequent offence with rigorous imprisonment of a term of not less than 6 months but which may extend to 7 years and with fine.

The approval of Commissioner of Income-tax is necessary to launch prosecution for offences under section 275, 276 A, 276 B, 276 C, 276 CC, 276 D, or 277 or 278 A, against any person. The Commissioner may compound any such offence (279). All the offences mentioned in Section 279 shall be deemed to be non-cognizable under the code of Criminal Procedure 1973.

14. **Punishment not to be imposed in certain cases** (Section 278 AA). Notwithstanding anything contained in Section 276 A, 276 AB or Sec. 276 B, no person shall be punishable for any failure referred to in the aforesaid provisions if he proves that there had been a reasonable cause for such failure.

15. **Offences by Companies** (Sec. 278 B). Where an offence under the Act has been committed, by a company, *every person* who, at the time offence was committed, was incharge of, and was responsible to the company for the conduct of

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the business as well as company shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

Such a person shall not be held liable to any punishment if he proves that the offence was committed without his knowledge or that he has exercised all due diligence to prevent the commission of such offence.

Section 278B (2) says that notwithstanding anything contained in sub-section (1) where an offence by a company under this Act is committed and it is proved that the offence has been committed with the consent or connivance of or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary, or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Explanation: Explanation attached to this section has defined the following:

(*a*) "Company" means a body corporate and includes—

(*i*) a firm; and

(*ii*) an association of persons or a body of individuals whether incorporated or not; and

(*b*) "director", in relation to—

(*i*) a firm, means a partner in a firm;

(*ii*) any association of persons or a body of individuals, means any member controlling the affairs thereof.

16. **Offences by Hindu Undivided Families.** (Section 278 C). For any offence committed by H.U.F., its Karta shall be liable for punishment and if any member was also involved, he shall also be punishable.

But if Karta can prove that the offence was committed without his knowledge or that he has exercised all due diligence to present the commission of such offence he can escape punishment.

17. **Presumption as to Assets, Books of Account etc. in certain cases.** (Sec. 278 D). Where during any search conducted u/s 132, any money, bullion, jeweller or other valuable article or thing or any books of account or other documents has or have been found in the possession or control of any person and such assets or books or documents are tendered by the prosecution in evidence against such person the provisions of Section 132 (4A) shall apply to such assets

Prosecution to be at the Instance of Commissioner [Sec. 279]

A person shall not be proceeded against for any offence under Sections 275 A, 276, 276 A, 276 B, 276 BB, 276 C, 276 CC, 276 D, 277, 278 except with the previous sanction of the Commissioner or Commissioner (Appeals) or the appropriate authority:

It is also provided that the Chief Commissioner or, as the case may be Director General, may issue such instructions or directions to the aforesaid income-tax authorities as he may deem fit for the institution of proceeding under this sub-Section. Appropriate authority shall have the same meaning as in Sec. 269 UA (C).

No prosecution u/s 276 or 277 shall be made in relation with assessment years in respect of which penalty has been reduced or waived by the Chief Commissioner or Commissioner. [279 (1A)].

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Any offence under this chapter may either before or after the institution of proceedings be compounded by the Chief Commissioner or Director General. [Section 279 (2)]

Where any precedings has been taken against any person, any statement made or account or other document produced by such person before any of the income-tax authorities shall not be inadmissible as evidence for the purposes of such proceedings merely on the ground that such statement was made or account or document was produced in the belief that the penalty imposable would be reduced or waived under section 273 A or that the offence in respect of which such proceeding was taken would be compounded. [Section 279 (3)]

Explanation: Finance (No. 2) Act, 1991 has added the following explanation—

For the removal of doubts, it is hereby declared that the power of the Board to issue orders, instructions or directions under this Act shall include and shall be deemed always to have included the power to issue instructions or directions (including, instruction or directions to obtain the previous approval of the Board) to other income-tax authorities for the proper composition of offences under this section.

Certain offence to be Non-Cognizable [Section 279 A]

Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), an offence punishable under Section 271 B or Section 276 C or 276 CC or 277 or 278 shall be deemed non-cognizable without the meaning of that code.

Proof of Entries in records or documents [Section 279 B]

In case income-tax auhorities submit in original or an authenticated copy of any entry in records or documents which are in their custody, it shall be admitted as evidence in any proceedings for prosecution under this chapter.

Disclosure of Information by Public Servants [Section 280]

A public servant contravening the provisions of Section 138 (2) shall be punishable with imprisonment extending upto six months and shall be liable to fine. The prior approval of Central Government is essential before instituting any prosecution under this section.

SUMMARY OF PROVISIONS RELATING TO PROSECUTIONS

Section	*Nature of Offence*	*Punishment*
275 A	For removing any asset, books of accounts, documents etc. found during search in contravention of order served under sec 132(3).	Imprisonment upto 2 years and fine.
276	For removal, concealment, transfer or delivery of property to avoid tax recovery.	Imprisonment upto 2 years and fine.
276 A	For default on the part of liquidator.	Imprisonment of 6 months to 2 years.
276 AB	For failure to comply with provision regarding transfer of immovable property	Imprisonment of 6 months to 2 years and fine.

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Section	Nature of Offence	Punishment
276 B	For failure to pay the tax deducted at source.	Imprisonment of 3 months to 7 years and fine.
276 BB	For failure to pay the tax collected at source.	Imprisonment of 3 months to 7 years and fine.
276 C(1)	For wilful attempt to evade tax, penalty, interest etc.	If tax evaded exceeds Rs. 1 lacs fine and imprisonment of 6 months to 7 years ; Otherwise fine and imprisonment of 3 months to 3 years.
276 CC	For failure to furnish Return of Income.	If tax evaded exceeds Rs. 1 lacs fine and imprisonment of 6 months to 7 years ; Otherwise fine and imprisonment of 3 months to 3 years.
276 CCC	For failure to furnish Return of Income in search cases u/s 158 BC.	Imprisonment of 3 months to 3 years and fine.
276 D	For failure to produce accounts and documents.	Imprisonment upto one year and fine of Rs. 4 to Rs. 10 for every day of default.
277	For false statement of verification.	If tax evaded exceeds Rs. 1 lacs fine and imprisonment of 6 months to 7 years ; Otherwise fine and Imprisonment of 3 months to 3 years.
278	For abelment in false return.	If tax evaded exceeds Rs. 1 lacs fine and Imprisonment of 6 months to 7 years ; Otherwise fine and Imprisonment of 3 months to 3 years.
278 A	For punishment of second and subsequent offences.	Fine and Imprisonment of 6 months to 7 years for every offence.

QUESTIONS

1. What are the different penalties which can be imposed under the provisions of Income-tax Act, 1961 ?
2. What are the different offences which make an assessee liable to prosecution ?
3. Discuss the provisions regarding the levy of penalties imposed on an assessee under the Income-tax Act as regards the following:
   (*a*) Failure to furnish information regarding securities;
   (*b*) Failure to furnish return and comply with notice; and
   (*c*) Failure to pay advance tax.

(B.Com. Punjab)

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PART VI

REVISIONAL PROBLEMS
(ASSESSMENT YEAR 1997-98)

1. REVISIONAL PROBLEMS WITH SOLUTIONS [PROBLEM 1 TO 17]
2. REVISIONAL PROBLEMS WITH HINTS [FOR SOLUTIONS TO THESE PROBLEMS PLEASE SEE OUR BOOK "PRACTICAL INCOME-TAX" (12TH EDITION 1997)] [PROBLEM 1 TO 50]

   PROBLEMS HAVE BEEN SOLVED IN RELATION TO

   PREVIOUS YEAR ... ENDING ON 31-3-97 AND

   ASSESSMENT YEAR ... 1997-98
3. OBJECTIVE TYPE QUESTIONS
4. SHORT QUESTIONS
5. VERY SHORT QUESTIONS

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1 REVISIONAL PROBLEMS WITH SOLUTIONS

Problem 1. Shri Prasad is employed in a public limited company on monthly salary of Rs. 4,000. He contributes to a provident fund which is recognised by the Commissioner of Income-tax at $12^1/_2\%$ of his salary. A similar amount is contributed by the employer. Interest credited to his provident fund account during the year is Rs. 1,200. The accumulated balance to his credit is Rs. 20,000. Two children of Shri Prasad are studying in the institution run by the employer for which no fees are paid. Normal expenditure per student in such institution is Rs. 65 per month.

The assessee is provided with a rent-free unfurnished accommodation owned by the employer, the municipal valuation of which is Rs. 12,000 per annum. He is provided with a gardener for the upkeep of the garden which is attached to the house. The wages paid by the company to the gardener amount to Rs. 1,500 only. He is also provided by the employer a car of 14 horse power rating on condition that its running and maintenance expenses will be borne by Shri Prasad.

What will be his salary income? *(Jabalpur University, B. Com.)*

Solution

Computation of salary Income of Sri Prasad

		(Amount Rs.)
Salary @ Rs. 4,000 p.m. for the year		48,000
Employer's contribution to the R.P.F. in excess of 10% of his salary (6,000–4,800)		1,200
Education expenses of his two children @ Rs. 65/- per month each		1,560
Rent-free Unfurnished House:		
Municipal Valuation Rs. 12,000 + 1,500=13,500		
10% of the salary *i.e.* 10% of Rs. 48,000=4,800		
Add (13,500–24,000)	Nil	4,800
Car of 14 H.P. rating provided by the employer. Its running and maintenance expenditure is borne by the assessee: @ Rs. 200 p.m.		2,400
Gross Salary		57,960
Standard deduction: (Maximum)		18,000
Salary Income		39,960

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Rebate u/s 88: Qualifying amount
Employee's own contribution to R.P.F.
@ $12^1/_2$ of salary ($12^1/_2$% on Rs. 48,000) 6,000

Notes: 1. Interest on R.P.F. balance is exempted as it is below prescribed rate.
2. The wages of the gardener, Rs. 1,500, paid by the company are not taxable as perquisite according to the circular of the Central Board of Direct Taxes dated 16-3-1974 but is to be added in F.R.V.

Problem 2. Ram Lal owns several properties, the annual value of which amount to Rs. 25,000 including Rs. 7,000 for a bungalow, where he resides. He claims the following expenses in respect of let-out houses.

Rs. 100—for insurance premium paid.
Rs. 1,400—for two year's interest on mortgage.
Rs. 500—for vacancy allowance.
Rs. 25—for ground rent.
Rs. 10—for land revenue.
Rs. 1,200—for collection charges.

Municipal taxes in respect of property let are Rs. 4,000 and for self-occupied house are Rs. 700/-

—Ascertain his taxable income assuming that he has no other income.

Solution

Computation of taxable income of Mr. Ram Lal

	Rs.	Rs.
Rental value of let out property (Rs. 25,000 – 7,000)		18,000
Less: Municipal Taxes		4,000
Net Annual Value		14,000
Deductions:		
(*i*) 1/5th for repairs	2,800	
(*ii*) Insurance Premia	100	
(*iii*) Ground rent	25	
(*iv*) Vacancy allowance	500	
(*v*) Land Revenue	10	
		3,435
Income from let-out house		10,565
Self-occupied House:		
Fair Rental value		7,000
Less : Municipal Taxes		700
Gross A.V.		6,300
Reduced to Nil u/s 23(2)		6,300
Income		Nil

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Income from House Property [10,565 + Nil] = 10,565

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Problem 3. The following particulars are furnished by an assessee for the accounting year ending 31st March, 1997

Machinery:	Rs.
Written Down Value on 1-4-96	40,000
Additions during the year (1-7-96)	20,000
Total	60,000
Factory Building:	
Written Down Value 1-4-96	2,00,000
Additions during the year (1-6-96)	50,000
Total	2,50,000

The machine worked triple shift throughout the year. Calculate the amount of depreciation admissible for the assessment year 1997-98 and the written down value on 1-4-97 (the rate of depreciation for machinery is 25% and for Factory Building is 10%). *(B. Com., Punjab)*

Solution

Depreciation	Rs.	Rate	Dep. Rs.
Normal Depreciation:			
Machinery W.D.V. on 1-4-96	40,000		
Additions during the year 1-7-96	20,000		
	60,000	25%	15,000
W.D.V. of Machinery on 1-4-97, 60,000–15,000 = 45,000			
Factory Building :			
W.D.V. on 1-4-1996	2,00,000		
Additions during the year	50,000		
	2,50,000	10%	25,000
W.D.V. of factory building as on 1-4-97	2,50,000–25,000 = 2,25,000		
Total Depreciation to be allowed during the assessment year 1997-98	15,000 + 25,000 = 40,000		

Problem 4. A Jute Mill Co. closes its books on 31st March each year. From the following information work out the amount of depreciation admissible for the assessment year 1997-98.

The total cost of machinery on 31st March, 1997 is Rs. 9,00,000 which includes cost of new machinery purchased on 1-4-93 for Rs. 1,00,000 and on 1-4-96 for Rs. 2,00,000. Total amount of depreciation claimed in respect of this asset upto and including the 1996-97 assessment year is Rs. 1,50,000. The rate of depreciation on the machinery asset is 25% in the year 1996-97, the whole of the machinery was

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employed for double shift working for 100 days and triple shift for another 100 days.
(Adapted from B. Com., Punjab)

Solution

Calculation of Depreciation admissible as deduction	Rs.
The total cost of the Machinery upto 31-3-1997	9,00,000
Less: Additions made during the year 1996-97 [1.4.96]	2,00,000
Cost of machinery upto 31-3-96	7,00,000
Less: Depreciation charged upto 31-3-96	1,50,000
W.D.V. on 1-4-1996	5,50,000
Add: Additions made on 1-4-96	2,00,000
W.D.V. on 31.3.1997 (Before dep.)	7,50,000
Normal Depreciation @ 25% of Rs. 7,50,000	1,87,500
W.D.V. on 1-4-97	5,62,500

Problem 5. From the following profit and loss account of a firm for the period ending on 31-3-97 ascertain the taxable profits from *business and the gross total income.*

Profit and Loss Account

	Rs.		Rs.
Office salaries	10,000	Gross Profit	58,000
Proprietor's salary	5,000	Profit on sale of property	20,000
Interest on proprietor's capital	2,000	Bad Debts recovered (not allowed by I.T.O. in previous year for lack of profit)	5,000
General expenses	5,000	Interest from Govt. securities (gross)	4,000
Bad debts	2,000	Dividends from Agricultural companies (gross)	2,000
Advertisements	4,500	Interest from Post Office Saving Bank	2,000
Fire Insurance premium	2,000		
Depreciation	4,000		
Reserve for sales tax	10,000		
Income-tax on last assessment	4,000		
Advance income-tax paid	2,000		
Donation to Punjab University	1,000		
Legal charges for defending a suit for alleged breach of a trading contract	500		
Motor car expenses	1,000		
Net Profit	38,000		
	91,000		91,000

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General expenses include Rs. 1,000 paid as compensation to an old employee whose services were terminated as his continuing in service was considered detrimental to the profitable conduct of the company's business and Rs. 200 by way of help to a poor university student. The depreciation is found to be in excess by Rs. 1,800.

The advertisement cost includes calendars and diaries Rs. 2,000. Motor car expenses include Rs. 500 attributable to private use of the car. The assessee has received demand notice of sales tax for earlier year amounting to Rs. 10,000 and he has not disputed the liability. *(Adapted from B.Com., Punjab)*

Solution

Computation of firm's Business Income		Rs.
Net profit as per given in the Profit and Loss Account		38,000
Add: Inadmissible deductions	Rs.	
Proprietor's Salaries	5,000	
Interest on Capital	2,000	
Income-tax	4,000	
Advance tax paid	2,000	
Donations to Punjab University	1,000	
Excess Depreciation	1,800	
Help to poor university student	200	
1/2 Motor Car Expenses (Personal)	500	
Reserve for Sales Tax	10,000	
		26,500
		64,500
Less: Incomes credited but not taxable		
Bad debts recovered	5,000	
Interest from Post Office Saving Bank	2,000	
		7,000
		57,500
Less: Incomes credited but Chargeable under other heads:		
1. Profit on sale of property	20,000	
2. Income from other sources		
Interest on Govt. Securities	4,000	
3. Dividends from Agricultural Co.	2,000	
		26,000
Profit from Business		31,500
Computation of Gross Total Income		
1. Profits from business		31,500
2. Capital Gains (sale of property)		20,000
3. Income from Other Sources: Dividends	2,000	
Interest on securities	4,000	
		6,000
Gross Total Income		57,500

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Notes: 1. Liability of sales tax, though existing and undisputed by the assessee, is not allowed as it has not been actually paid [Section 43 B].

2. Bad debts recovered are the income of the year in which they are recovered but they were not previously allowed by the I.T.O. ; as such they are not taxable now.

Problem 6. Bhupendra Mohan is a practising Chartered Accountant. He keeps his accounts on cash basis and his summarised cash account for the year is as under:

	Rs.		Rs.
To Balance b/d	9,014	By Office expenses	4,150
,, Audit Fees	14,750	,, Institute Exp.	902
,, Income from other accountancy work	5,475	,, Personal Exp.	519
,, Institute fees	2,100	,, Membership and Certificate fees	143
,, Examiner's fee	645	,, Life Insurance premium	1,250
,, Interest on Govt. Securities (Net)	4,500	,, Income-tax	2,493
,, Rent from property (Not subject to any local taxes)	4,300	,, Motor car purchased	30,000
		,, Motor car expenses	420
		,, Insurance of property	300
		,, Balance c/d	607
	40,784		40,784

Having regard to the following information, compute his total income for the previous year.

(*a*) Office expenses include Rs. 173 for the purchase of technical books for office.

(*b*) One-third of motor-car expenses are in respect of his professional practice.

(*c*) His all investments are in Government securities.

(*d*) Depreciation allowance for motor-car and furniture is Rs. 6,452.

Solution

Computation of total income of Mr. Bhupendra

I. *Professional Incomes:*

	Rs.	Rs.	Rs.
(*i*) Audit fees	14,750		
(*ii*) Income from other accountancy work	5,475		
(*iii*) Institute fees	2,100		
(*iv*) Examiner's fees	645		
		22,970	
Less: Allowable Professional expenses:			
Office expenses	4,150		
Institute Expenses	902		
Membership and Certificates fees	143		
Motor Car expenses (being 1/3rd share)	140		

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Depreciation	Rs.		
Motor Car 1/3rd	2,000		
Furniture	452		
	2,452		
		7,787	
Professional Income			15,183
II. *Income from Property*			
Rental Value		4,300	
Less: Municipal Taxes		Nil	
Net Annual Value		4,300	
Deductions:			
1/5 of Annual Value as repairs	860		
Insurance Premium	300		
		1,160	
			3,140
III. *Income from Other Sources*			
Interest (Net Rs. 4,500, Gross 4,500 × 100/90)			5,000
Gross Total Income			23,323
Deductions: u/s 80 L:			
Interest from Government securities			5,000
Total Income			18,323

Rounded off to Rs. 18,320

Notes : 1. Depreciation on car will be = 30,000 × 20/100
= 6,000
Depreciation on Furniture = 6,452– 6,000 = 452.

2. *Q.A. for rebate u/s 88 :* Life Insurance Premium Rs. 1,250.

Problem 7. The gross total income of Mr. Bahl, a citizen of India, amounts to Rs. 1,00,000. The following further details are provided by him:

1. Premium paid by him on his life insurance policy of Rs. 40,000 amounted to Rs. 5,000. He also paid a premium of Rs. 500 on a policy on the life of his minor son.
2. Contribution to recognised Provident Fund—Rs. 600.
3. Deposits in a 10 year account under the Post Office Savings Bank (C.T.D.) Rules—Rs. 1,200.
4. Contribution to Public Provident Fund—Rs. 700.
5. During the year he has paid Rs. 3,000 by cheque as Medical Insurance Premium under MEDICLAIM.

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6. Donation to Daya Nand Medical Hospital
   [Rs. 3,000 for Family Planning purposes] Rs. 5,500
   Donation to Punjab University Rs. 2,500
   Help to a poor student Rs. 1,000
7. During the year, he has spent Rs. 18,000 on the medical treatment of his one handicapped child in a nursing-home. The child was in the nursing-home for 200 days.
8. The G.T.I. includes dividends to the tune of Rs. 12,000.
9. The Gross Total Income also includes the following items

	Rs.
(*a*) Long-term capital gains:	
(*i*) from the sale of land	8,000
(*ii*) from the sale of shares	1,000
(*b*) Short-term capital gain	1,000
(*c*) Winning from lotteries	7,500

Compute his total income.

Solution

Computation of Total Income of Mr. Bahl

	Rs.	Rs.
Gross Total income (as given)		1,00,000
Less: Winning from Lotteries	7,500	
Capital Gains (Long Term)	9,000	
(Short Term)	1,000	
Dividends	12,000	
		29,500
Income from other heads		70,500
Capital Gains		
Short Term Capital Gain	1,000	
Long Term Capital Gain	9,000	
		10,000
Other Sources:		
Winning from Lotteries	7,500	
Less : Exempted u/s 10(3)	5,000	
	2,500	
Dividends	12,000	
		14,500
G.T.I.		95,000
Deductions u/s 80:		
u/s 80 D: Medical Insurance Premium	3,000	
u/s 80 DD: Medical treatment of handicapped	15,000	

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u/s 80 L : Dividend		12,000	
u/s 80 G: Donations: Punjab University	2,500		
Hospital	5,500		
	8,000		
Q. A. = 10% of			
[95,000 – (3,000 + 15,000 + 12,000 + 9,000)]			
∴ Q.A. = 5,600: Rate:			
For Family Planning @ 100%	3,000		
Rest Rs. 2,600 @ 50%	1,300		
		4,300	
			34,300
Total Income			60,700

Notes : 1. *Rebate u/s 88 :* Qualifying Amount

(*i*)	L.I. Premium on his own life	5,000
(*ii*)	Minor son's life	500
(*iii*)	C.T.D.	1,200
(*iv*)	Own Contribution to R.P.F.	600
(*v*)	Public Provident Fund	700
	Q.A.	8,000

2. Help to a poor student does not qualify for deduction u/s 80G.

Problem 8. The details of the income of Mr. Vinod for the previous year ending 31st March, 1997 are given below:

Indian Income

(*i*) Interest from government securities Rs. 1,500.

(*ii*) A loss of Rs. 3,000 under the head "Income from House Property" has been computed.

(*iii*) Share of income from an A.O.P. Rs. 25,000. (None of its members pays tax).

(*iv*) Dividends (Net) Rs. 3,200.

(*v*) Share of income from a Hindu undivided family as member thereof Rs. 2,000.

(*vi*) Dividend on Units of Unit Trust of India Rs. 5,000.

Foreign Income

(*i*) Income from money-lending business in England but received in India Rs. 3,000.

(*ii*) Income arising in Pakistan from a business (controlled from India) Rs. 5,000 and from house property Rs. 1,000.

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(*iii*) Income earned from bank interest in Pakistan and received there but remitted to India in the previous year Rs. 3,000.

(*iv*) Rs. 20,000 brought into India during the previous year out of untaxed income arising in America before the previous year.

During the previous year he paid Rs. 2,000 on the Medical Insurance Premium. He also paid Rs. 10,000 as premium on his life insurance.

Compute his total income for the assessment year 1996-97 in case (*i*) he is resident, (*ii*) he is not ordinarily resident, and (*iii*) he is non-resident in India.

Solution

Computation of Mr. Vinod's Income

		Resident	*Not Ordinarily Resident*	*Non-Resident*
		Rs.	Rs.	Rs.
Indian Income:				
(*i*) *Business Income:*				
Share of income from an A.O.P.		25,000	25,000	25,000
(*ii*) *Income from other Sources:*				
Dividend (Net 3,200)				
Gross up (3,200 × 100/80)	4,000			
Dividends on Units	5,000			
Int. on Govt. Securities	1,500			
		10,500	10,500	10,500
(*iii*) Loss under the head House Property, (will be set off against income under other heads)		(–) 3,000	(–) 3,000	(–), 3,000
		32,500	32,500	32,500
Foreign Income:				
(*i*) Money lending business income from England but received in India		3,000	3,000	3,000
(*ii*) Income from business in Pakistan (controlled from India)		5,000	5,000	—
(*iii*) Income from House Property in Pakistan		1,000	—	—
(*iv*) Income earned from Bank interest in Pakistan and received there		3,000	—	—
(*v*) Past year's untaxed income brought in India from America		—	—	—
Gross Total Income		44,500	40,500	35,500

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Deductions:
u/s 80D:
Medical Insurance Premium 2,000
u/s *80L:*
Deduction on investment
(3,000+4,000+1,500+2,000)= 10,500
10,500

	12,500	12,500	12,500
Total Income	32,000	28,000	23,000

Notes: (*i*) Income from A.O.P. is also eligible for rebate.
(*ii*) Share of Income received from H.U.F. is exempted.
(*iii*) *Rebate u/s 88 :* Q.A.
—Life Insurance Premium 10,000.

Problem 9. The following particulars are submitted by Mr. Godse. Compute his gross total income.

Salary Rs. 10,000; bonus Rs. 3,000; enjoys free use of the car of 16 h.p rating. He contributes 10% of his salary to a recognised provident fund. The company contributes @ 11% to it. He employs a gardener whose salary is paid by the company, Rs. 1,000. p.a.

He is owner of a house with the rental value of Rs. 4,000. He incurs these expenses; local tax Rs. 800; fire insurance premium Rs. 200; ground rent Rs. 1,000. Interest on borrowed money Rs. 4,500.

One more house is owned by him but this is let out on a rent of Rs. 5,000 per annum. Municipal taxes in respect of this house amount to Rs. 500 and the collection charges Rs. 300. The house remained vacant for three months. Mr. Godse has paid interest of Rs. 4,120 on the loan which was used for the construction of the house.
(B.Com., Punjab)

Solution

Computation of Gross Total Income of Mr. Godse.

	Rs.	Rs.
I. *Salary*		
Salary	10,000	
Bonus	3,000	
U/s 17(2) (*iv*) gardener's salary paid by the employer	1,000	
Excess of employer's contribution to R.P.F. over 10% of Salary (1,100 – 1,000)	100	
Gross Salary	14,100	
Standard Deduction u/s 16 (*i*) $33^1/_3$% of 14,100	4,700	
		9,400

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II. *House Property:* Let out House			
Annual Rental value		5,000	
Less : Municipal Taxes		500	
		4,500	
Annual Value			
Deductions:	Rs.		
(*i*) 1/5th for repairs	900		
(*ii*) Interest on Loan	4,120		
(*iii*) Vacancy Allowance 4,500 × 3/12	1,125		
		(–) 6,145	
Loss from this house to be set off		(–) 1,645	
Self-occupied house: ARV	Nil		
Less: Interest on Borrowed money	(–) 4,500		
Loss from self-occupied house		(–) 4,500	
			(–) 6,145
Gross Total Income			3,255

Notes: 1. The perquisites of Motor Car is not taxable as the salary of the employee does not exceed Rs. 24,000.

2. A deduction regarding interest on borrowed money shall be allowed upto Rs. 10,000 out of the Annual Rental value of the self-occupied house. It will be set off from income of other heads.

3. Loss from let out house property can be set off from other heads.

Problem 10. Mr. A.N. Aiyer has been the Sales Manager since 1-4-50 of Messers Right & Co. Ltd. The following are the particulars of his income:

	Rs.	
Salary	3,000	p.m.
Dearness Allowance	300	,,
Entertainment Allowance (Before 1-4-55 he was getting Rs. 6,000 p.a.)	8,000	p.a.
Employer's contribution to Recognized Provident Fund (equal to employee's own contribution)	4,000	,,
Life Insurance premium paid on his own life	8,500	,,
Interest credited to Provident Fund calculated @ 13% per annum	3,900	,,

He is provided with a car of 12 h.p., all expenses for maintenance and running are also met by the employer. It is used partly for business and partly for personal purposes.

He is the owner of a house which is let-out for Rs. 4,800 per annum since it was constructed in April, 1968. Total Municipal Annual Tax is Rs. 400.

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His other Incomes are as follows:

(*i*)	Accrued Interest on NSC's	Rs. 6,000
(*ii*)	Dividend	Rs. 3,000
(*iii*)	Bank Interest	Rs. 5,000

One of his daughters is mentally retarded and he has to spend Rs. 1,500 p.m. on her medical treatment. During the year he donated Rs. 5,000 to an institution which is looking after mentally retarded children and this institution is an approved body.

Find out his total income.

Solution

	Computation of Total Income Mr. A.N. Aiyer		Rs.
I.	Salary @ Rs. 3,000 p.m.		36,000
	Dearness allowance @ Rs. 300 p.m.		3,600
	Entertainment allowance		8,000
	Excess of employer's contribution to recognised provident fund over 10% of employee's salary: (4,000 – 3,600)		400
	Interest credited to R.P.F. over 12% (3,900 – 3,600)		300
	Perquisite: Motor Car, 12 h.p. (Expenses met by employer) @ Rs. 600 p.m.		7,200
	Gross Total Salary		55,500
	Standard Deduction u/s 16 (*i*) (Maximum)	18,000	
	Entertainment allowance u/s 16 (*ii*) (as computed in notes)	6,000	
			24,000
	Salary Income		31,500
II.	*Income from House Property*		
	Annual Rental Value	4,800	
	Less: Municipal Taxes	400	
	Annual Value	4,400	
	Deduction: Repairs, 1/5 of Annual Value	880	
	Income from House property		3,520
III.	*Income from other sources:*		
	Accrued Interest on NSC's	6,000	
	Dividend	3,000	
	Bank Interest	5,000	
			14,000
	Gross Total Income		49,020
	Deductions:		
	u/s 80 DD: Expenses on Medical treatment of a handicapped child	15,000	

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u/s 80 L:			
Accrued Interest on NSC	6,000		
Bank Interest	5,000		
Dividend from Indian companies	3,000		
		14,000	
u/s 80 G: Donations			
Donations given Rs. 5,000			
Q.A. 10% of [49,020 – (14,000 + 15,000)]			
Rs. 2,002 Rate 50%		1,001	
			30,001
Total Income			19,019
Rounded off to Rs. 19,020			
Rebate u/s 88: Q.A.—			
Life Insurance Premium		8,500	
Contribution to RPF		4,000	
Accrued Interest on NSCs		6,000	
Q.A.		18,500	

Note: Deduction u/s 16 (*ii*): Entertainment allowance
Least of the following:

(*i*) Rs. 7,500;

(*ii*) 1/5th salary *i.e.*, 36,000 = Rs. 7,200;

(*iii*) Amount of E.A. received before 1-4-55 = 6,000 (Least);

(*iv*) Amount of E.A. being received now—Rs. 8,000.

Problem 11. Mr. Sober's particulars of income are given below. Compute his salary income.

Salary @ Rs. 3,000 p.m.

Bonus equal to 2 months' salary.

Employee contributes $12^1/_2$% of his salary towards his Recognised Provident Fund. The employer also contributes the same amount.

Interest credited in the Recognised Provident Fund @ 9% is Rs. 20,000.

The employer provided him house rent allowance of Rs. 500 p.m. and the employee pays a rent of Rs. 700 p.m.

The employee is provided with a big car which he utilises for his official as well as private purposes.

The employee went to England in connection with his official work and stayed there for 2 months. He also took his family with him. The employer had borne the air passage of the employee *i.e.*, Rs. 5,000 and of his family Rs. 18,000.

The employee pays Rs. 10,000 as L.I.C. premium on the policy of Rs. 75,000. His wife is also insured for 20,000 and he pays a premium of Rs. 1,500 p.a.

He is also contributing Rs. 100 p.m. in 10 year C.T.D. Scheme.

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Solution

Computation of salary income of Mr. Sobers

	Rs.	Rs.
Salary @ Rs. 3,000 p.m.		36,000
Bonus equal to 2 months' salary		6,000
Employer's Contribution to R.P.F.	4,500	
Exempted upto 10% of salary	3,600	
		900
Interest credited to R.P.F. (Exempted as it is below prescribed rate)		Nil
Air passage money spent by the employer on the family of the employee		18,000
Car perquisite for 10 months @ Rs. 800 p.m.		8,000
House Rent Allowance:		
(*i*) 40% of salary	14,400	
(*ii*) Actual H.R.A. received	6,000	
(*iii*) Rent paid exceeding 10% of salary (8,400 – 3,600) (Least)	4,800	
H.R.A. taxable (6,000 – 4,800)		1,200
Gross Salary		70,100
Deduction u/s 16 (*i*) Maximum		15,000
Salary Income		55,100

Rebate u/s 88: Qualifying Amount	
P.F. contribution	4,500
Life Insurance Premium:	
Self	10,000
Wife	1,500
10-year C.T.D.	1,200
Q.A.	17,200

Notes: 1. As the employee went to England on business tour, air passage for his journey is not taxable. But the passage money of family borne by the company is taxable.

2. During his stay outside India for 2 months, the assessee did not use the car. It is assumed that expenses are met by employer.

Problem 12. Mr. D. Mohan is employed at Mysore in private concern and is in receipt of following emoluments:

Salary Rs. 2,000 p.m.

Dearness Allowance Rs. 400 p.m.

Entertainment Allowance Rs. 500 p.m.

Bonus Rs. 2,000 p.a.

Rent-free furnished house: Annual Rental Value of unfurnished house is Rs. 5,000 and Cost of furnishing Rs. 30,000.

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He is a member of Recognised Provident Fund to which he contributes 10% of his salary and his employer contributes Rs. 3,200 p.a. Interest credited to his account on accumulated balance @ 8% is Rs. 3,000. He deposited Rs. 250 p.m. to a 10-year C.T.D. Account and pays a premium of Rs. 3,000 p.a. on his own life.

Calculate his total income.

Solution

Calculation of total income of Mr. D. Mohan

	Rs.	Rs.	Rs.
Income from Salary			
Salary @ Rs. 2,000 p.m.		24,000	
D.A. @ Rs. 400 p.m.		4,800	
Entertainment allowance Rs. 500 p.m.		6,000	
Bonus		2,000	
Perquisite: Rent-free Furnished House:	Rs.		
A.R.V. of unfurnished house: 5,000			
10% of Salary (24,000 + 6,000 + 2,000)	3,200		
Add: Excess of F.R.V. over 50% of salary (Mysore)	Nil		
Value of unfurnished House	3,200		
Add: 10% of cost of furnishing (10% of Rs. 30,000)	3,000		
		6,200	
Excess of employer's contribution in R.P.F. over 10% of salary (3,200 – 2,400)		800	
Interest on accumulated balance (Exempted)		Nil	
Gross salary			43,800
Standard Deduction u/s 16 (i)			
$33^1/_3$% of Rs. 43,800			14,600
Salary Income being Total Income			29,200

Rebate u/s 88

Qualifying amount	Rs.
1. Contribution to R.P.F.	2,400
2. Premium on Life Insurance	3,000
3. Contribution to C.T.D.	3,000
Q.A.	8,400

Problem 13. Mrs. Fancy Rose has given the following information about her income. She requests you to find out her Gross Total income for the assessment year 1997-98:

	Rs.
(*a*) Salary from M/s. Glaxo Ltd.	24,000
(*b*) Dividends on DCM shares (gross)	1,500

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(*c*)	Interest on securities (gross)	6,000
(*d*)	Interest on Fixed Deposits in PNB	3,200
(*e*)	Profit from agency business	10,000
(*f*)	Loss from speculation of shares	10,000
(*g*)	Profit from speculation in silver	5,000
(*h*)	First Prize in Delhi State Lotteries	1,00,000
(*i*)	Gain from playing Rummy in the club	2,000
(*j*)	Loss in flash (card game) with friends	3,000
(*k*)	Loss in race course bettings	10,000
(*l*)	Expenses incurred on maintenance of horses	30,000

(B.Com., Punjab)

Solution

Computation of Gross Total Income

		Rs.	Rs.
Salary Income			
Salary		24,000	
Less: Standard Deduction $33^1/_3$% of 24,000		8,000	
			16,000
Profit & Gain from Business or Profession:			
Profit from agency Business		10,000	
Speculation Loss in shares	Rs. 10,000		
Speculation Profit in silver	Rs. 5,000		
To be carried forward	Rs. 5,000		
		Nil	
			10,000
Other Sources:			
Lotteries (Rs. 1,00,000, *Less* : exempted 5,000)		95,000	
Gain from Rummy		2,000	
Loss from flash (Rs. 3,000)			
[This loss can neither be adjusted nor can be carried forward]			
Interest on fixed deposits		3,200	
Dividends		1,500	
Interest on securities		6,000	
			1,07,700
Gross Total Income			1,33,700

Notes: 1. Loss in race course betting cannot be set off from any other income and also cannot be carried forward.

2. Expenses incurred on maintenance of horses can be carried forward to be set off only from gain of horse races.

Problem 14. Sh. Ram Prasad Aggarwal is manager of a H.U.F. consisting of his two brothers and a major son. He has submitted following particulars regarding the Income of H.U.F.

1. Profit from the business carried on by Mr. Aggarwal on behalf of H.U.F. (After deducting Rs. 5,000 paid as salary to Mr. A.P. Aggarwal, brother

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and Rs. 10,000 to Mr. R.P. Aggarwal for acting as salesman and Rs. 8,000 have been paid to Mr. R.P. Aggarwal was his salary for managing the business) is Rs. 80,000.

2. Family owns a house whose rental value is Rs. 9,000 Municipal Taxes paid in respect of it are Rs. 900 and the house is used for the residence of family. Fire Insurance Premium paid Rs. 1,000.
3. Life Insurance Premium paid by Karta.
   (*i*) On his own life Rs. 6,000 on a policy of Rs. 50,000.
   (*ii*) On joint life with his brother Rs. 10,000 on a policy of Rs. 80,000.
4. Interest from Tax-free debentures of a Sugar Mill Co. (Unlisted) (Net) Rs. 4,800.
5. Loss from speculation business—Rs. 2,000.

Compute the total income of H.U.F.

Solution

Computation of total income of the H.U.F. managed by Mr. R.P. Aggarwal.

	Rs.	Rs.
1. *House Property:* Self occupied Net Annual value is taken as	Nil	Nil
2. *Income from Business:* Business Profit	80,000	
Speculation loss Rs. 2,000 (To be carried forward)	—	
3. *Income from Other Sources:* Interest on securities 4,800 × 100/80		6,000
Gross Total Income being Total Income		86,000

Rebate u/s 88: Qualifying Amount:

(*i*) Life Insurance Premium—Self	6,000
(*i*) On Joint life with Brothers:	10,000
Q.A.	16,000

Problem 15. Ram, Shyam and Jadu are partners in a firm, sharing profits and losses in the proportion of 3 : 2 : 1 respectively. The Profit and Loss Account of the firm for the year ending 31st March, 1997 is as under:

	Rs.		Rs.
To Sundry Trade Expenses	25,000	By Gross Profit	1,40,000
„ Reserve for B/debts	10,000		
„ Income Tax	5,000		
„ Rent of business premises (paid to Ram)	10,000	„ Dividend (Net)	10,000
„ Interest on Capital @ 12%			
Ram	3,000		
Shyam	2,000		
Jadu	1,000		

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,, Salary to Shyam	6,000	
,, Commission to Jadu	3,000	
,, Net profit	85,000	
Total	1,50,000	1,50,000

Income-tax amounting to Rs. 2,500 has been deducted at source on dividend income.

Compute total income of the firm. The firm has submitted its partnership deed alongwith the return for the assessment year 1997-98. It contains payment of interest on capital to partners and salary and commission to Shyam and Jadu who are working partners.

Solution

Computation of firm's total income

	Rs.	Rs.	
I. *Firm's Business Income:*			
Net Profit as per P & L A/c		85,000	
Add: Expenses not allowed:			
(*i*) Reserve for B/Debts	10,000		
(*ii*) Income Tax	5,000		
(*iii*) Salary to Shyam	6,000		
(*iv*) Commission to Jadu	3,000	24,000	
		1,09,000	
Less: Income chargeable to tax under Other heads: Dividend		10,000	
Firm's Book Profit			99,000
Less : Allowable remuneration u/s 40 (*b*): [6,000 + 3,000]			9,000
Business Income			90,000
II. *Income from other Sources*			
Dividend (Net)		10,000	
Add: Tax deducted at source		2,500	
			12,500
Firm's Total Income			1,02,500

Notes:

1. Interest on capital paid to partner is allowed as rate of interest is below 18%.
2. Salary and commission paid to working partners is allowed u/s 40 (*b*) as it is given as per deed.
3. Int. on capital, salary and commission received by partners is their taxable income under the head profits and gains.
4. Shares of income from such firm, received by partners is exempted u/s 10(2A).
5. Firm is not eligible for deduction u/s 80I.

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Problem 16. A and B are active partners while C and D are sleeping partners in a PFAOP. The following is the Profit and Loss Account of the PFAOP for the year ending on 31st March, 1997:

P & L A/c

	Rs.		Rs.
To Rent and Taxes	4,000	By Gross Profit b/d	70,000
,, Salaries	14,000	,, Miscellaneous Receipts	1,000
,, Postage	1,000		
,, Commission	2,000		
,, Interest	20,000		
,, Travelling Expenses	5,000		
,, Net Profit transferred to—			
Rs.			
A 6,250			
B 6,250			
C 6,250			
D 6,250			
	25,000		
Total	71,000	Total	71,000

Notes: 1. Rent and Taxes include Rs. 1,200 paid to A as rent for premises let out by him for PFAOP's business.

2. Salaries include payments to following partners:

A	5,000
B	3,000
	8,000

3. Interest includes amounts allowed on partner's capital as follows:

A	2,000
B	4,000
C	6,000
D	3,000
	15,000

The private incomes of the partners are as follows:

(*i*)	A	15,000
(*ii*)	B	6,000
(*iii*)	C	8,000
(*iv*)	D's share in an A.O.P.	22,000

Treating the firm as A.O.P., find out the taxable income of each partner.

Solution

Computation of total income of firm assessed as AOP

	Rs.	Rs.	Rs.
Net profit as per P & L A/c			25,000
Add: Expenses not allowed:			

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Salaries to partners:			
A	5,000		
B	3,000		
		8,000	
Interest to partners:			
A	2,000		
B	4,000		
C	6,000		
D	3,000		
		15,000	
			23,000
PFAOP's Total Income			48,000

	Allocation Amongst Partners			
	A	B	C	D
	Rs.	Rs.	Rs.	Rs.
Salary	5,000	3,000	—	—
Interest on Capital	2,000	4,000	6,000	3,000
Share of PFAOP's Profit	6,250	6,250	6,250	6,250
Share of PFAOP's Income	13,250	13,250	12,250	9,250
Individual Incomes	15,000	6,000	8,000	22,000
(Rent from property)				
Rs.				
A. V. = 1,200				
Less: 1/5th for				
repairs = 240				
	960	—	—	—
Gross Total Income being Total Income	29,210	19,250	20,250	31,250

Note : This share will be fully added in the individual income of partners and they can claim rebate of tax u/s 86. PFAOP will pay tax at the rates applicable to an individual as total income of partners does not exceed Rs. 40,000.

Problem 17. How will you deal with the following claims under the Income-tax Act ?

(*a*) A company makes a donation of Rs. 10,000 to the Government for propagation of family planning and claims it as an allowable expense.

(*b*) Company, which is neither a banking nor a financial company, has received deposits from public and has paid in the year 1996-97 as interest of Rs. 2,50,000. It claims that the whole expenditure has to be allowed.

(*c*) A company claims deduction for remuneration of Rs. 1,35,000 (inclusive of perquisites of Rs. 45,000) paid to its whole time director.

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(*d*) X, an individual, who discontinued his profession as a lawyer in 1994 received Rs. 25,000 in May; 1996 from one of his past clients as arrears of fees. He claims that since no profession was carried on by him in 1996 so the receipt is exempt from tax. X has been assessed on his professional income in all the past years on cash basis.

(*e*) Y, Chartered Accountant, rendered professional assistance to a leading industrialist. He was offered a remuneration of Rs. 25,000 for these services, which he declined to receive, but however requested that this might be paid to a charitable organisation, which the industrialist did. Y says that since he did not receive the amount, he is not taxable on the amount. *[C.A. (Inter) Nov., 1979]*

Solution

(*a*) In this case if donations for family planning are within 10% of the Company's Gross Taxable Income, then the company shall be allowed a deduction u/s 80 G @ 100% of donations made.

(*b*) The company shall be allowed a deduction of Rs. 2,50,000 as restriction u/s 40 A (8) has been deleted.

(*c*) Full amount of salary and perquisites can be debited to P & L A/c because ceiling u/s 40 A (5) has been deleted with effect from assessment year 1991-92.

(*d*) As he was paying tax on cash basis, hence he had not paid tax on this income when it was due. Hence, it shall be taxable as professional income in the assessment year 1997-98.

(*e*) Only that income which is diverted under a legal charge is not taxable in the hands of the assessee. In the present problem it is voluntary application and hence taxable.

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2 REVISIONAL PROBLEMS WITH HINTS

SALARIES

Problem 1. S, an individual, employed by a company, draws a salary of Rs. 3,000 per month. His employer gives him the choice of one of the two alternatives as given below:

(*i*) getting a rent free unfurnished house at Delhi for which the rent is Rs. 1,000 per month and the company will pay, that rent, or

(*ii*) getting a cash house rent allowance of Rs. 1,000 per month.

S having to find out his own accommodation at Delhi and pay the requisite rent.

S opts for the second alternative and takes the cash house rent allowance of Rs. 1,000 per month. He takes house in Delhi at a rent of Rs. 800 per month.

Has he made a wise choice? Discuss. *(P.U., M.Com.)*

[**Hints:** *If he opts for House Rent Allowance*—Taxable portion of H.R.A. is Rs. 6,000]

If he opts for rent-free Accommodation. Value of rent-free accommodation to be added in salary is Rs. 3,600. If he opts for house rent allowance he has to pay tax on a higher amount of Rs. 2,400 but at the same time he will still have a saving of Rs. 2,400. As such his choice is wise].

Problem 2. Arun an employee of company at Calcutta is given the choice of either accepting house rent allowance at Rs. 5,000 p.m. or rent free infurnished accommodation having fair rental value of Rs. 5,000 p.m. If he accepts HRA he will have to pay rent at Rs. 5,000 per month himself. His salary other than the facility of house or HRA is fixed at Rs. 6,000 p.m. Which one of the two options should he accept ? *(B.Com. P.U. April, 1995)*

[**Hints:** He can opt for any option as his salary income in both the cases shall be same *i.e.* Rs. 81,000. Value of rent-free House is Rs. 24,000 and Taxable HRA is also Rs. 24,000]

Problem 3. On retirement after 20 years of continuous service on December 31, 1996 an employee received the undernoted sums.

(*i*) Retirement gratuity of Rs. 40,000 based on one month's salary for each year of service. His salary in 1991 was Rs. 1,600 p.m. since when it had

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increased @ Rs. 100 p.m. each year. His salary is due on the last day of every month.

(*ii*) A sum of Rs. 75,000 from an unrecognised provident fund, the composition being:

Employee's Contribution	30,000
Interest thereon	7,500
Employer's Contribution	30,000
Interest thereon	7,500
	75,000

State giving reasons what amounts, if any, out of the above noted receipts are chargeable to income-tax in the assessee's hands in the relevant assessment year. *[M.Com., P.U.]*

[**Hints:** (*i*) Average monthly salary Rs. 2,100; Exempted amount Rs. 21,000; Taxable gratuity Rs. 19,000.

(*ii*) Employer's contribution and interest thereon shall be taxable in the year in which he retires (30,000 + 7,500 = 37,500).

(*iii*) Interest on his own contribution *i.e.*, Rs. 7,500, is taxable as income from other sources.]

Problem 4. The following particulars are submitted by Mr. Deshpande for the assessment year 1997-98. You are required to compute his gross total income.

(*a*) Salary Rs. 30,000, bonus Rs. 3,000, enjoys free use of a car of 16 h.p. rating. He and his employer both contribute to a recognised provident fund @ 11% of his salary.

(*b*) He is the owner of a house with a rental value of Rs. 8,000. He incurs these expenses : local taxes Rs. 800, fire insurance premium Rs. 200, ground rent Rs. 1000. The house is self-occupied.

(*c*) One more House is owned by him but that is let out on a rent of Rs. 5,000 per annum. Muncipal taxes Rs. 500 and collection charges Rs. 300. The house remained vacant for two months. Interest on a loan taken for the construction of this house Rs. 4,000. *(B.Com. P.U. April, 1995)*

[**Hints :** Salary Income Rs. 22,200 (car exempted) ; House Property loss to be adjusted Rs. 1,150 ; Gross total Income Rs. 21,050]

Problem 5. Mr. Kamal Kant Kapoor was appointed lecturer in commerce in Punjab Agricultural University in the grade of Rs. 2,200-75-2,800-100-4,000 and on 1-1-1994 his pay was fixed at Rs. 2,200 p.m. He is provided with a rent-free accommodation which is a three-room set having municipal valuation of Rs. 6,000 p.a. The Fair Market value of the accommodation is Rs. 600 p.m. He contributes @ 10% of this salary to his provident fund to which his employer also contributes the same amount. He is getting dearness allowance @ 70% of his salary. Due to illness of his son, the University reimbursed medical bills of Rs. 5,750 during the year. Salary falls due on 1st of every month.

Mr. Kapoor also claims the following deductions from his gross salary.

(*i*) Maintenance expenses of his car which is of 12 H.P., Rs. 3,000.

(*ii*) Rs. 600 deposited in 10-year C.T.D. scheme.

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(*iii*) Rs. 1,200 paid to L.I.C. on his policy of Rs. 10,000.

(*iv*) He invested Rs. 12,000 in March, 1997 in Equity Linked Saving Scheme of U.T.I.

(*v*) He donated Rs. 5,000 towards Chief Minister's Drought Relief Fund.

Calculate Mr. Kapoor's total income for the assessment year 1997-98.

[**Hints:** Salary Rs. 28,350 (2,350 × 10 + 2,425 × 2) Valuation of rent free house 10% of salary; Salary income Rs. 34,020; Deduction u/s 80 G Rs. 1,701 Total Income Rs. 32,319; Q.A. for rebate Rs. 14,635]

Problem 6. The particulars of income of Mrs. P, the Accountant of M. Co. Ltd. during the year are as under:

(*i*) Salary @ Rs. 5,000 per month.

(*ii*) Contribution to a recognised Provident Fund @ 10% of salary by both the employer and the employee.

(*iii*) Provision of a 14 H.P. car together with a driver, all expenses being met by the employer. The car is used by Mrs. P *for personal as well as employment purposes.* The total cost incurred by the employer is Rs. 12,000 in this regard. The employer also claims depreciation of Rs. 2,000 on the car.

(*iv*) A free furnished house belonging to M. Co. Ltd. is given to Mrs. P for her residential accommodation in Bombay. One-third space is used for official work. The fair rent of the whole house should be Rs. 900 per month. The Company incurs repair expenses of Rs. 3,000. The furniture belongs to the employer and was acquired at a cost of Rs. 36,000. Depreciation of Rs. 3,500 is claimed by the employer on the building and furniture.

(*v*) Medical expenses of Rs. 2,500 incurred by Mrs. P were met by M. Co. Ltd.

(*vi*) Mrs. P paid insurance premium of Rs. 9,500 on a policy on her own life of value Rs. 80,000. During the year she received dividends (gross) of Rs. 5,800 from an Indian Company and interest of Rs. 800 from a scheduled bank.

(*vii*) During the year she deposited Rs. 4,000 is N.S.S. and spent Rs. 16,000 on medical treatment of her handicapped dependent son.

From the above noted data, compute giving reasons :

(*a*) Mrs. P's gross total income, and

(*b*) Q.A. for rabate u/s 88 *(Punjab M.Com.)*

[**Hints:** Value of rent-free furnished accommodation—Rs. 8,400; Gross salary—Rs. 79,200; Gross Total Income—Rs. 67,800; Deduction u/s 80 DD Rs. 15,000 80 L—Rs. 6,600. Total Income—Rs. 46,200. Q.A. for rebate u/s 88 Rs. 19,500. Cost of furnishing & F.R.V. are taken as 2/3 of total cost. No account to be taken of expenses on repair, depreciation of the building, furniture etc. Since for how much time the car is used for private purposes is not known, so the perquisite of car is to be calculated according to the statutory limits and no account is taken of the expenses incurred on car and its depreciation]

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Problem 7. Shri A, a Sales Executive of Public Limited Company at Madras, received the following incomes and perquisites:

(*i*) Salary —Rs. 2,500 per mensem

(*ii*) Dearness Allowance as per the terms of employment (Rs. 500 p.m. enter into pay for computation of service benefits) —Rs. 1,000 per mensem

(*iii*) Employer and employee's contribution to R.P.F. @ —Rs. 350 p.m. each

(*iv*) Interest credited on balance to the credit of Shri A in Provident Fund account @ 10% —Rs. 1,000

(*v*) Entertainment Allowance granted regularly since 1954 —Rs. 7,500 per annum

(*vi*) Motor Car 20 H.P., running and maintenance expenses incurred by the employer (wholly used by the employee). It is conceded by the I.T. Dept. that 50% of the running of car is for official purposes. —Rs. 9,800 p.a.

(*vii*) Rent-free accommodation. Rent paid by the employer —Rs. 1,000 per mensem

(*viii*) Professional Tax paid by the employee —Rs. 200

(*ix*) Dividends (Gross) —Rs. 2,400

(*x*) He received Rs. 10,000 as royalty from a book written in Hindi which is a university text book.

(*xi*) Accrued interest on N.S.C. (VIII issue) is —Rs. 4,000.

Assuming that he has paid an Insurance premium of Rs. 2,500 on a policy of Rs. 30,000; paid Rs. 2,000 by cheque to get himself medically insured. Indicate the reliefs due to him. Tax need not be calculated.

Compute his total income.

[**Hints:** Value of house 3,750; Car perk 50% of actual expenses: 4,900; Gross salary 58,750; Deduction u/s 16 (*i*) 18,000 16 (*ii*) 6,000: 16 (*iii*) Rs. 200 Salary Income 34,550; other sources 16,400: G.T.I. Rs. 50,950; U/s 80 D Rs. 2,000; 80 L Rs. 6,400, and 80 QQA Rs. 2,500; Total Income Rs. 40,050; Q.A. for rebate u/s 88 Rs. 10,700]

Problem 8. Mr. Jacob, General Manager of a Limited Company of Bombay, furnishes the following particulars in respect of his income:

(*i*) His net salary per month was Rs. 3,000 after deduction of income-tax Rs. 3,500 p.a. and own contribution to office Provident Fund.

(*ii*) His annual contribution to Recognised Provident Fund was Rs. 6,000 and his employer paid double the amount as contribution.

(*iii*) Bonus at 20% of salary.

(*iv*) Entertainment Allowance Rs. 10,000 p.a. receiving since 1.4.1954.

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(*v*) He is provided with well furnished bungalow of the company the fair rent of which is Rs. 20,000 and cost of furnishing Rs. 40,000.

(*vi*) The value of medical bill reimbursed for him and his family by the company was Rs. 3,000.

(*vii*) Refreshment during office hours, Rs. 1,000, provided by the company.

(*viii*) He made a holiday trip to a hill station with his four dependents under leave travel concession. All railway tickets amounting to Rs. 3,000 were met by employers.

(*ix*) He is provided with 20 H.P. Motor car by the company for his personal use. The maintenance cost of car is borne by the company which amounts to Rs. 6,000 p.a.

(*x*) He has a policy of Rs. 1,50,000, premium paid was Rs. 17,000.

(*xi*) He paid Rs. 10,000 to a hospital to promote family planning.

(*xii*) He earned Rs. 30,000 from a poultry farm which he is running at his village.

(*xiii*) His other incomes are:

(*a*)	Bank Interest	Rs. 8,000
(*b*)	Dividend from Indian companies	Rs. 4,000
(*c*)	Interest on units of U.T.I.	Rs. 2,000

(*xiv*) He got himself medically insured and paid Rs. 5,000 as premium.

Compute the Total Income of Mr. Jacob.

[**Hints:** Gross Salary Rs. 87,760; Value of rent-free accommodation Rs. 9,710; Railway Ticket—Tax free; excess of employer's Contribution (12,000 – 4,550) = Rs. 7,450; Deduction u/s 16 (*i*) Rs. 15,000 & u/s 16 (*ii*) Rs. 7,500; Salary Income Rs. 65,260; Business Income Rs. 30,000; Other sources Rs. 14,000 GTI 1,09,260 Deductions u/s 80 D Rs. 5,000; 80 JJ Rs. 10,000; 80 L Rs. 14,000 and 80 G Rs. 8,026 Total Income 72,234; Q.A. for rebate u/s 88 Rs. 23,000]

Problem 9. Mr. "A", Manager of M/s. Clay & Co., Nagpur, has furnished the following particulars in respect of his income:

		Rs.
(*i*)	Duty pay for eleven months	4,000 p.m.
(*ii*)	Leave salary for June	4,000
(*iii*)	I.T. deduction at source	350 p.m.
(*iv*)	Dearness allowance—This does not enter into computation of his superannuation or retirement benefits	400 p.m.
(*v*)	Entertainment allowance He has been receiving this allowance regularly from this Company since 1-4-1953. The amount of the allowance was however Rs. 400 p.m. upto 31-3-56. Rs. 500 p.m. from 1-4-56 to 31-3-86 and Rs. 700 p.m. thereafter.	700 p.m.

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(*vi*) He is provided with rent-free furnished accommodation. The Company pays rent of Rs. 1,500 p.m. for the accommodation and has furnished it at a cost of Rs. 22,000.

(*vii*) Salaries of the gardener, Rs. 200 p.m. and chowkidar, Rs. 250 p.m., paid by the Company.

(*viii*)	Dividends (Gross) from an Indian Co.	1,200
(*ix*)	Contribution to recognised Provident Fund	500 p.m.
(*x*)	Employer's contribution to above	500 p.m.
(*xi*)	Interest credited at 9% per annum on the balance balance to his credit in the Provident Fund	3,850
(*xii*)	Contribution to Public Provident Fund	1,000
(*xiii*)	The following payments were made by him during the year:	
	(*a*) Premium on own life policy for a sum of Rs. 10,000.	2,000
	(*b*) Premium on a policy on the life of his wife for a sum of Rs. 10,000	1,000
	(*c*) Premium paid on policy taken under Children's Endowment Policy Scheme	500
	(*d*) Premium paid on policy on his own life for Rs. 20,000 which has been reimbursed to him by his employer	500
	(*e*) Premium paid for insurance of household goods	500
	(*f*) Amount paid under the Cumulative Time Deposit Scheme:—	
	— in 10-year Deposit Scheme in the name of his minor son	1,800
	(*g*) Professional tax	850
	(*h*) Books purchased which are necessary for the purposes of his duties	700
	(*i*) He maintained a 14 H.P. car purchased in 1976, which was used for the purposes of his employment.	

Compute his salary income for the year and qualifying amount u/s 88.

[**Hints:** Value of rent-free accommodation Rs. 7,360; Gross Salary Rs. 73,140; Deduction u/s 16 (*i*) Rs. 15,000 & u/s 16 (*ii*) Rs. 4,800; 16 (*iii*) 850; Salary income Rs. 52,490; Dividend (gross) Rs. 1,200; G.T.I. Rs. 53,690; 80L Rs. 1,200; Total Income Rs. 52,490; Q.A. for Rebate u/s 88 Rs. 12,800]

Problem 10. From the particulars of Mr. Samesesame, given below, you are required to compute his salary income.

Basic salary Rs. 19,000; High Cost of Living allowance 20% of the salary: Entertainment allowance Rs. 5,600; Conveyance allowance Rs. 6,000; Family allowance Rs. 2,000; Profit bonus @ 30% of the salary; Rent-free unfurnished accommodation with a fair rent of Rs. 2,000 p.m.

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The other particulars are:

(*i*) He contributes @ 12% to an Unrecognised P.F.

(*ii*) He pays life insurance premium amounting to Rs. 5,000 the capital sum assured being 40,000.

(*iii*) 80% of the conveyance allowance was stated to have been spent in discharging of official duties.

(*iv*) Prior to 1st April, 1955, Mr. Samesesame used to get entertainment allowance @ Rs. 250 p.m. *(P.U. B. Com.)*

[**Hints:** Value of rent-free house Rs. 11,800; Gross Salary Rs. 49,100; Deduction u/s 16 (*i*) Rs. 16,367, u/s 16 (*ii*) Rs. 3,000; Salary being T.I. Rs. 29,733: Q.A. for rebate u/s 88 Rs. 5,000. Family allowance is fully taxable and enters into pay for valuation of rent-free house. High cost of living allowance being another name of D.A. D.A. does not enter into pay for valuation of house]

Problem 11. Sh. Sanjay resident of Delhi, submits the following details of income for the financial year 1996-97 :

(*i*) Salary Rs. 5,600 p.m.

(*ii*) D.A. Rs. 600 p.m.

(*iii*) Entertainment allowance Rs. 600 p.m. (prior to 1-4-55 he was getting Rs. 200 p.m.)

(*iv*) City compensatory allowance Rs. 200 p.m.

(*v*) Bonus Rs. 6,000.

(*vi*) Employer's contribution to RPF Rs. 8,000. His own contribution is also Rs. 8,000.

(*vii*) Interest on the accumulated balance of the fund @ 10% p.a. Rs. 28,000.

(*viii*) He is provided with an unfurnishsed house for which the employer charges Rs. 400 p.m. the municipal value of the house being Rs. 16,000 p.a.

(*ix*) He is also provided with a chauffeur driven 18 H.P. car which he can use for his private purposes. Running and maintenance cost met by employer.

(*x*) During the year he has received dividend from an Indian Co. amounting to Rs. 6,400 (Net)

(*xi*) His profit from a speculation business Rs. 20,000.

(*xii*) He owns a house which has been let out @ Rs. 1,000 p.m. Its annual municipal value is Rs. 10,000. Municipal taxes are Rs. 1,000.

(*xiii*) He contributed Rs. 4,000 in ULIP and purchased NSC's (*VIII* issue) worth Rs. 6,000 in the previous year. The interest accrued on NSC's (VIII issue) purchased in earlier years amounted to Rs. 2,400. He donated Rs. 2,000 towards Prime Ministers National Relief Fund.

Compute his taxable income for the assessment year 1997-98.

(B.Com. P.U. April, 1995)

[**Hints :** Value of concessional rent house Rs. 3,240; Salary Income Rs. 90,320; H.P. Rs. 8,800 P & G. Rs. 20,000 ; Other Sources Rs. 10,400; Deduction u/s 80L, Rs. 10,400 u/s 80G, Rs. 2,000 Total Income Rs. 1,17,120 Q.A. for rebate u/s 88 Rs. 20,400]

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HOUSE PROPERTY

Problem 12. Mr. A is the owner of three house properties at Cuttack, particulars in respect of which are as below:

	1st House	2nd House	3rd House
1. Construction started	1-4-86	1-8-72	1-7-60
2. Construction completed on	31-12-91	30-9-74	31-12-60
3. Actual rent received	Rs. 4,800	1,000	Dwelling House
4. Municipal Rental value	Rs. 3,600	1,000	18,000
5. Municipal Taxes paid by the owner	Rs. 240	40	1,800
6. Municipal Taxes paid by the tenant	Rs. —	40	—
7. Cost of repairs borne by	owner	owner	owner
8. Vacancy period	—	—	4 months
9. Collection charges	Rs. 60	35	—
10. Insurance Premium	Rs. 20	15	360
11. Interest on loan taken for the repairs of house	Rs. 250	200	3,600

Mr. A's income from other sources is Rs. 1,00,000.

During the previous year, Mr. A had to stay at Kanpur for 4 months in connection with his business obligation and during this period, his dwelling house remained vacant. During his stay in Kanpur he did not occupy any other house of his own.

Calculate the house property income.

[**Hints:** Income from House No. I = 1,218, II = 553. Loss from III House Rs. 3,600. Loss from house property Rs. 1,829]

Problem 13. Mr. Sanjay is the owner of four house properties. Calculate his income under the head house property.

(*i*) The first house the municipal valuation of which is Rs. 5,000 is in Mr. Sanjay's self-occupation.

(*ii*) The second house is let-out to a hosiery business at a monthly rent of Rs. 600. This house was built in the year 1981 and for this he took a loan of Rs. 12,000 from a friend at an interest of 10% p.a.

(*iii*) The third house was built on 1st January, 1997 and since then it is let out for residential purposes at a monthly rent of Rs. 2,000 p.m. Collection charges paid Rs. 600. Annual charge which Mr. Sanjay created in favour of his younger brother is Rs. 10,000.

(*iv*) The fourth house is let out at a rent of Rs. 400 p.m. Unrealised rent (fulfilling all the conditions) is Rs. 10,000.

The municipal taxes in case of all the four houses are Rs. 500 p.a. Rs. 700 p.a. Rs. 2,400 p.a. and Rs. 400 p.a. respectively.

Mr. Sanjay's income from all other sources is Rs. 30,000.

[**Hints:** Income from First House Rs. Nil; Second House Rs. 4,000; Third house Rs. 4,320; Fourth House after making deduction of unrealised rent (–), 6,480. Income from house property Nil + 4,000 + 4,320 – 6,480 = 1,840]

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Problem 14. Mr. Ramcharan is the owner of following house properties. Calculate his house property income.

(*i*) His first house is at Amritsar built in 1951 and let-out at present @ Rs. 450 p.m. Other expenses are:

Repairs Rs. 2,000; Ground rent Rs. 100; Insurance premium for the year which is yet to be paid Rs. 200.

(*ii*) He owns another house at Ludhiana in which he stays himself. Municipal Value of this house is Rs. 7,200. During the year he met the following expenses:

Repairs Rs. 1,000. Interest paid on borrowed money Rs. 2,000. Annual charge which he created himself in favour of his uncle Rs. 200 p.m.

(*iii*) He also constructed a house which has two units at Chandigarh on 31st January, 1992. One of which is let-out at Rs. 600 p.m. and in other one his son is living without paying any rent. Expenses incurred by him are: repairs Rs. 500, ground rent Rs. 500, fire insurance premium Rs. 200. Let-out portion remained vacant for two months.

His income from all other sources Rs. 20,000.

[**Hints:** First house Rs. 4,220; Third house: 1st unit vacancy allowance 2/12th of Rs. 4,200 = 700; Income 2,310 2nd unit Rs. 5,410 = 7,720; Second house Nil. Loss from this House Rs. 2,000, *i.e.*, upto, interest paid on borrowed money. No deduction of unpaid insurance premium and self-created annual charge. Income from H.P. Rs. 9,940]

Problem 15. Mr. A owns a property which consists of three identical flats. Construction of the property started in 1981 and on completion the property was occupied for the first time on September 30, 1991. Two flats are let-out on rent of Rs. 1,300 each per month and the third is occupied by Mr. A himself. Other relevant details are given below:

	Rs.
Annual Municipal valuation of the property	40,000
Annual Municipal Tax	12,000
Ground Rent paid	2,000
Insurance Premium on Property	900

Mr. A had borrowed Rs. 20,000 against his fixed deposits to repair the tenanted portion of the property. He paid interest of Rs. 2,400 on the said loan. He had spent Rs. 2,000 for collection of rent. One of the rented flats remained vacant for a period of 2 months during the year.

Mr. A had the following other incomes:

	Rs.
Interest on fixed deposit with a Bank	4,000
Gross Dividend	1,000

Mr. A paid during the year Life Insurance Premium of Rs. 11,000. He also contributed Rs. 9,000 to the Public Provident Fund. Compute the total income of Mr. A.

[**Hints:** Income from let-out Flats Rs. 9,714; self-occupied Flat Nil; G.T.I. Rs. 14,714; Deduction u/s 80L—Rs. 5,000 Total Income 9,714, Q.A. for rebate u/s 88 Rs. 20,000]

Problem 16. From the following details, please compute the depreciation and other claims allowable to an assessee under the Income-tax Act, 1961. The unit is producing fertilizers.

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	Rs.
(*a*) Written down value of plant and machinery on 1-4-96	3,60,000
(*b*) Additions to plant made on 11-10-96	75,000
(*c*) Cost of machinery purchased on 1-1-97 but not installed	60,000
(*d*) Sale Proceeds of machinery which was originally bought on 1-4-94 for Rs. 84,000	1,00,000
(*e*) Machinery lost in a fire accident on 20-3-97 Original cost Rs. 25,000 when purchased on 1-8-95. Amount received from the insurance company—	15,000

The machinery is entitled to depreciation at 25%. All items of machinery have worked triple shift.

[**Hints:** W.D.V. on 1-4-96 Rs. 3,60,000; Less money realised (1,00,000 + 15,000). Add Cost of new P & M installed and used Rs. 75,000; Net W.D.V. 3,20,000; Dep. @ 25% of Rs. 2,45,000 for full year and on Rs. 75,000 for half year Rs. 70,625; No dep. to be allowed on P & M not yet installed. W.D.V. on 1-4-97 Rs. 2,49,375]

Problem 17. The books of a manufacturing concern disclose the following information:

Profit & Loss A/c

	Rs.		Rs.
To Opening Stock	3,38,000	By Sales	8,70,000
,, Purchases	3,29,900	,, Misc. Incomes	2,490
,, Stores consumed	21,800	,, Closing Stock	1,29,000
,, Power and Fuel	7,680		
,, Rates and Taxes	430		
,, Repairs to Machinery	9,070		
,, Repairs to Building	1,680		
,, Misc. Expenses	15,860		
,, Salaries and Wages	95,500		
,, Contribution to R.P.F.	6,200		
,, Staff Welfare Expenses	1,020		
,, Bonus	4,400		
,, Insurance	2,500		
,, Commission to Agents	43,500		
,, Selling Expenses	780		
,, Audit fees	980		
,, Bad debts	2,100		
,, Licence fee	1,090		
,, Interest	26,500		

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To Provision for Taxation	22,000	
,, Depreciation	40,000	
,, Net Profit	30,500	
	10,01,490	10,01,490

Notes: 1. Misc. expenses include:

(*i*) Penalty for violation of Foreign Exchange Regulations Rs. 1,200.
(*ii*) Expenses to defend a criminal case against managing director—Rs. 3,000.
(*iii*) Donations to P.M. Drought Relief Fund Rs. 2000.
(*iv*) Wealth tax paid—Rs. 3,000
(*v*) Donations to Mr. Singh—Rs. 5,000.

2. Bad debts include a sum of Rs. 500 for advances to suppliers of raw materials with whom assessee had exclusive arrangements for purchase of such materials.
3. Misc. incomes include refund of advance Income-tax—Rs. 400.
4. Allowable depreciation—Rs. 36,000.

From the above particulars, compute the business income of the concern.

[**Hints:** Business profit—Rs. 70,300. Refund of advance Income tax is not taxable. Penalty and expenses to defend a criminal suit are not allowed. Bad Debt of Rs. 500 cannot be claimed as bad debt but is allowed as expenditure u/s 37]

Problem 18. Following is the Profit and Loss Account of Sh. Biren Mitra for the year ending 31st March 1997. You are required to ascertain his income from business for the year ended on that date.

	Rs.		Rs.
To Salaries	10,800	By Gross Profit	35,672
,, Sundry Expenses	1,200	,, Discount	751
,, Reserve for Bad Debt	4,500	,, Commission	1,205
,, Insurance	450	,, Sundry Receipts	52
,, Advertising	2,500		
,, Income-tax	2,375		
,, Car Expenses	1,200		
,, Interest on Capital	1,000		
,, Interest on Bank Loan	1,550		
,, Charity	150		
,, Life Insurance Premium (self)	550		
,, Depreciation :			
On Building 1,000			
On Furniture 200			
	1,200		
,, Difference in Trial Balance	105		
,, Net Profit for the year	10,100		
	37,680		37,680

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This motor car was used equally for business purposes and the proprietor's private purposes.

The amount of depreciation allowable according to Income-tax Rules, in respect of Building and Furniture was Rs. 800 and Rs. 150 respectively. Included in the advertising expenses is a sum of Rs. 1,000 expended on a special advertising compaign undertaken during the year in respect of a product of a company placed recently in the market. Salaries include Rs. 6,000 being the amount drawn by Sh. Biren Mitra during the year against profits.

[**Hints :** Business Income Rs. 25,630; Expenditure on sale compaign allowed u/s 37]

Problem 19. Following are the particulars of Business income and depreciation for the previous years :

	1995-96	1996-97
	Rs.	Rs.
Profit from cycle business (before depreciation)	20,000	2,50,000
Depreciation	1,50,000	1,00,000
Profit from Hosiery Business (before depreciation)	65,000	10,000
Depreciation	10,000	20,000
Income from House Property	8,000	8,000

Calculate the income of Mr. R. for the assessment years 1996-97 and 1997-98.

[**Hints :** Assessment year 1996-97; Unabsorbed dep. C/F Rs. 67,000; G.T.I. Nil; Assessment year 1997-98; G.T.I. Rs. 81,000]

Problem 20. During the previous year 1996-97 an assessee sells the following assets

	Bonds (Listed)	Gold	Shares
Date of sale	March 31, 1997	April 10, 1996	May 17, 1996
Date of acquisition	April 10, 1992	June 3, 1977	April 10, 1991
	Rs.	Rs.	Rs.
Sale consideration	50,000	4,15,000	1,15,000
Cost of acquisition	44,000	60,000	55,000
Fair market value on April 1, 1981	—	— 69,000	—

Income from other sources Rs. 30,000, donation to approved charitable trust Rs. 4,000. The assessee deposits in the public provident fund Rs. 16,000. The cost inflation indices for the years 1981-82, 1991-92, 1992-93 and 1996-97 are 100, 199, 223 and 305 respectively.

Find out the tax liability of the assessee.

(B. Com. P.U. April 1995)

[**Hints :** L.T.C. Gain Gold Rs. 2,04,550, shares Rs. 30,704 L.T.C. Loss Bonds Rs. 10,179. Total L.T.C.G. Rs. 2,25,075. Other Income Rs. 30,000 Deduction u/s 80 G 1,500 Total Income Rs. 2,53,580 Tax @ 20% on Rs. 2,13,580 *i.e.*, Rs. 42,716. No rebate u/s 88]

Problem 21. Mr. Mahendra is shareholder in D.D. Ltd. He acquired 300 shares of the company of the face value of Rs. 100 per share in 1972. The fair market value

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of the shares as on 1-4-1981 was Rs. 200 per share. He made a further purchase of 200 shares at the rate of Rs. 300 per share in 1984-85. D.D. Ltd. issued bonus shares in 1987-88 in the proportion of 1 : 4.

X.Y. Ltd. another company, in a scheme of amalgamation made a proposal to acquire the shares of D.D. Ltd. as per offer given below :

Rs. 400 per share in cash plus 1 share in X.Y. Ltd. for every two shares of D.D. Ltd. The market value of shares of X.Y. Ltd. on the date of offer is Rs. 350 per share. Compute the capital gain, if any, arising to Mr. Mahendra if he accepts the offer. [C.I.I. for 1981-82 is 100, for 1984-85 is 125 and for 1996-97 is 305]

[Adapted C.A. (Final) November, 1991]

[**Hints :** Consideration Rs. 3,59,200; Cost Price Indexed Rs. 3,29,400 L.T.C. Gain = Rs. 29,800; Cost of Bonus shares Nil]

TOTAL INCOME OF INDIVIDUALS

Problem 22. Shri Kumar is a *film actor*. He has shown an income of Rs. 1,60,000 from profession and Rs. 40,000 from business which included a sum of Rs. 5,000 as profit on goods exported outside India. He also declared income of Rs. 10,000 from property. He claimed the following :

(*i*) Rs. 14,000 paid towards deposit in 15-year account under the Post Office Savings Bank (Cumulative Time Deposits) Rules, 1959;

(*ii*) Rs. 32,000 paid as life insurance premium on a policy for Rs. 3,00,000 taken in the name of his wife in June, 1986; and

(*iii*) He deposited Rs. 6,000 in N.S.S.

(*iv*) He donated Rs. 40,000 to a hospital approved u/s 80 G;

(*v*) He also earned Rs. 1,00,000 from a foreign country, as he was a member of cultural troupe that toured America. He brought foreign exchange worth Rs. 80,000 in convertible foreign exchange.

Compute total income of Shri Kumar.

[**Hints :** HP Income Rs. 10,000 Business profit Rs. 3,00,000 Deduction u/s 80 HHC Rs. 5,000; u/s 80 RR Rs. 60,000 u/s 80 G Rs. 12,250 Total Income Rs. 2,32,750 Q.A. u/s 88 Rs. 52,000]

Problem 23. Shri S. of Rajasthan State Service posted at Jaipur showed the following in his return of income :

		Rs.
(*a*)	Salary	36,000
(*b*)	Interest on securities (gross)	3,000
(*c*)	Property (annual value)	7,200
(*d*)	Dividend (gross)	12,000

The following claims are made :

(*i*) Rs. 6,000 contribution to Provident Fund and Rs. 5,000 life insurance premium on Mrs. S's life.

(*ii*) Purchased books costing Rs. 600 which were necessary for his duties.

(*iii*) He has house property at Karnal which is let-out at the rate of Rs. 2,000 p.m. It was completed in 1978 and Rs. 4,000 are claimed for Municipal

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House-tax and Rs. 2,000 for repairs and Rs. 6,000 for interest on borrowed money.

(*iv*) He donated Rs. 2,000 to Rajiv Gandhi Foundation and distributed milk worth Rs. 3,000 to patients in hospital at Jaipur.

(*v*) He is living in a rented house at Jaipur and paying Rs. 1,500 p.m. as rent.

(*vi*) He has deposited Rs. 10,000 in N.S.S. 1992.

The assessee has not shown in the return Rs. 6,000 entertainment allowance received from the State claiming it to be exempt.

Calculate the total income of Shri S with an explanatory note where necessary.

[**Hints :** Salary Income Rs. 23,000; Income from house property 10,000; Other sources Rs. 15,000; G.T.I. Rs. 48,000 Deductions 80 GG Rs. 8,750, 80 L Rs. 12,000 and 80 G Rs. 1,000 Total Income Rs. 26,250; Q.A. for rebate u/s 88 Rs. 21,000]

Problem 24. Compute the total income of Mr. X who has furnished the following particulars :

				Rs.
1. Salary				12,000
2. Income from property (Situated in Calcutta)				
Rent receivable—		Rs.		
Property B		7,000		
Property C		6,200		
			13,200	
Less : Expenses :				
Municipal taxes				
	Rs.			
Property A	600			
Property B	1,200			
Property C	1,400			
		3,200		
Repairs of Property :				
Property A	400			
Property C	300			
		700		
Interest on mortgage of property B (at 6% on Rs. 20,000)		1,200		
Insurance premium :				
Property A	100			
Property B	150			
Property C	200			
		450		
Collection charges		2,400		
			7,950	
				5,250
				17,250

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Notes : 1. The assessee has settled in Bombay for the purposes of his employment where he resides in a rented house.

2. Property A is required for self-occupation and property B and C are let out.

3. The assessee was on leave for 3 months during the previous year and during this period he resided in the property. Rest of the period house remained vacant.

4. Loan of Rs. 20,000 on mortgage of property B was used for agricultural purposes.

5. The Municipal rental values of house A, B and C are Rs. 3,000. Rs. 6,000 and Rs. 7,200 respectively.

[**Hints :** Salary Income Rs. 8,000; House B Rs. 4,490; House C Rs. 4,440; House A Nil; Total Income Rs. 16,930]

Problem 25. Radhey Shyam is manager in a firm. The particulars of his income are as follows :

		Rs.
(*i*)	Monthly Salary and D.A.	2,500
(*ii*)	Car Allowance @ Rs. 250 per month	
(*iii*)	Commission on net profits after charging his commission @ 5% (Profits before charging his commission Rs. 3,50,000 for the year ended 31.3.1997)	
(*iv*)	Net income from Royalty from a book written in 1993 in Bengali	
	He claims Rs. 2,000 as expenses	12,000
(*v*)	Sale proceeds of a private car	14,000
(*vi*)	$^1/_2$ Share of profit from an A.O.P.	20,000
(*vii*)	Agricultural income	10,000
(*viii*)	His other incomes are :	
	(*a*) Dividend from Indian Company	4,000
	(*b*) Interest on Bank Deposits	4,000
	(*c*) Interest on Govt. Securities	2,000

Find out total income of Radhey Shyam if he makes the following savings out of his income :

(*a*) He contributes 10% of his salary to a recognised P.F. to which his employer contributes 20%.

(*b*) Pays Insurance Premium of Rs. 2,000 on his own Policy for Rs. 18,000.

(*c*) He invests Rs. 8,000 in CANPEP which is eligible u/s 88;

(*d*) He donates Rs. 5,000 to a recognised scientific research institute; and

(*e*) He met with an accident 2 years back and lost one of his eyes.

[**Hints :** Salary Income Rs. 35,111, Business Income Rs. 20,000 other sources Rs. 20,000; G.T.I. Rs. 75,111 Deductions u/s 80 L Rs. 10,000; 80 U Rs. 40,000; 80 GGA 5,000 Total Income 20,111 Q.A. u/s 88 Rs. 13,000]

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Problem 26. Dr. D. is an E.N.T. Specialist. He has returned an income of Rs. 82,500 from his profession.

The following facts have been elicited during discussions :

(*a*) On his shareholding in an Indian Investment Company of Rs. 40,000 he received dividend at 10% partly made up of cash of Rs. 2,000 and partly by way of 20 shares of X Company Ltd. of face value of Rs. 100 each.

(*b*) Foreign tour expenses debited included Rs. 24,800 incurred by him on his visit to London to study the latest development in his line of profession and Rs. 21,400 on his visit to Vienna for consulting doctor there for his heart trouble. He was accompanied by his wife on both the visits.

(*c*) The assessee sold his ancestral residential house, where he was living since 1943 onwards for Rs. 2,20,000 on 28-3-96. The sale deed was executed on 2.4.1996. [C.I.I. = 305] He invested the sale proceeds in purchasing another house on 10.12.1996 for Rs. 1,15,000 with a plinth area of 5,000 sq. ft. of which 3,000 sq. ft. were rented out and the balance was used as his residence. The market value of his old house sold may be taken to be Rs. 62,000 as on 1.4.1981.

(*d*) He was subscribing to a Cumulative Time Deposit (10 years) scheme @ Rs. 200 per month.

(*e*) L.I.P. paid was Rs. 7,500.

(*f*) Bank interest received on S.B. account was Rs. 525.

Compute the total income of the assessee.

[**Hints** : (*i*) House property, Nil, (*ii*) Professional Income 82,500 + 12,400 + 21,400 = Rs. 1,16,300, (*iii*) Capital gain 30,900 but Fully exempted u/s 54 (*iv*) Other sources Rs. 4,525. Deductions : u/s 80L Rs. 4,525. Total Income Rs. 1,16,300; Q.A. for rebate u/s 88 Rs. 9,900]

Problem 27. Mr. P. Dayal, a Manager of a Tea Company, employed at Calcutta, supplies you the following information about his incomes :

(*i*) Income from Salary Rs. 2,000 p.m.

(*ii*) He is contributing 10% of his salary to a P.F. which is recognised; the company contributing 12%.

(*iii*) Interest credited to his P.F. account Rs. 1,740 at 9% rate of interest.

(*iv*) He is provided with a rent-free furnished residence the annual value of which was Rs. 15,000.
Rent of Furniture is Rs. 1,000 p.a.

(*v*) He is the owner of a house property in Calcutta and getting a monthly rent of Rs. 600. Local taxes paid by him amounted to Rs. 500 during the year. The house remained vacant for 2 months.

(*vi*) He had one fourth share in an A.O.P. whose total income being Rs. 48,000. [None of its member's income exceeds Rs. 40,000]

(*vii*) He had Rs. 2,500 as income from dividends on units of the Unit Trust of India.

(*viii*) He donated Rs. 5,000 to Calcutta University.

(*ix*) He was insured for Rs. 25,000 and paid Rs. 3,000 as premium.

(*x*) He maintains a Motor Car of 20 h.p., the expenditure on its running and maintenance were Rs. 5,500.

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Compute Mr. P. Dayal's total income. *[Nagpur, M.Com.]*

[**Hints :** Salary income Rs. 18,987, H.P. income Rs. 4,244, AOP Share of income Rs. 12,000, Dividend Rs. 2,500, G.T.I. = Rs. 37,731; Deduction u/s 80 G Rs. 1,162, 80 L—Rs. 2,500, Total Income Rs. 34,069 Eligible for rebate on share of income from firm assessed as AOP; Q.A. for rebate of tax u/s 88 Rs. 5,400]

Problem 28. Mr. Dutt, the Director of Prabhat Ltd., gives the following particulars of his income :

(*a*) Basic Salary at Rs. 2,500 p.m.

(*b*) Dearness Allowance at Rs. 800 p.m. (Rs. 500 p.m. enters into pay)

(*c*) Cash house rent allowance at Rs. 550 p.m.; he took a house in Bombay for his residential accommodation at a rent of Rs. 750 p.m.

(*d*) Director's Meeting fee Rs. 2,400.

(*e*) A motor car of 14 H.P. was provided by the employer for use by Mr. Dutt, partly in the performance of his duties and partly for his personal purposes but the expenses on maintenance and running for Mr. Dutt's personal purposes are met by Mr. Dutt.

(*f*) Premium of Rs. 6,000 on an insurance policy of Rs. 50,000 on Mr. Dutt's life was paid by the company.

(*g*) Mr. Dutt and the company each contributed $12^1/_2$% of the salary to a recognised provident fund.

(*h*) Mr. Dutt himself paid premium of Rs. 4,000 and Rs. 3,500 on two policies on his own life and his wife's life respectively.

Compute Mr. Dutt's total income. *[C.A. (Inter.)]*

[**Hints :** Salary Income Rs. 33,400; T.I. Rs. 35,800; Q.A. for rebate of tax u/s 88 Rs. 18,000]

Problem 29. From the following information, compute the assessable income of Mr. B.

(*i*) Income from the family business—Rs. 2,00,000.

(*ii*) Mr. B owns two houses, one built in January 1974 which he occupies himself and the second house comprises of 4 independent residential units built on 1st July 1991 which he has let out at Rs. 8,000 per mensem.

(*iii*) The house occupied by himself was inherited by him from his father who had stipulated that Mr. B should pay Rs. 5,000 per annum to his mother.

(*iv*) To construct let-out house, he had to borrow money for which the annual interest payments work out to be Rs. 8,000 and the annual repayment of loan is Rs. 20,000.

(*v*) The rateable value of the self-occupied house is Rs. 54,000 whereas of the let out flats is Rs. 1,08,000. In computation of these rateable values the municipal authorities deduct a notional 10%.

(*vi*) Over and above the rent mentioned in (*ii*) above, his tenants have also agreed to reimburse one-half of municipal taxes.

(*vii*) During the previous year the following expenses are incurred by Mr. B in respect of the two houses—

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	Self-occupied Rs.	Let out Rs.
Building repairs	5,000	2,000
Ground rent	3,000	4,000
Collection Charges	—	1,200
White washing	1,000	1,000
Fire Insurance Premium	400	600
Municipal Taxes	8,200	12,000

[I.C.W.A. (Final)]

[**Hints :** White-washing is to be treated as repairs expenditure. Fair Rental Value = Rateable value × 100/90. Income from self-occupied house Nil; Income from let out House Rs. 75,720; Total Income Rs. 2,75,720]

Problem 30. A retired from Government service and took up a job with a company thereafter. The following are the particulars of his income, etc. for the financial year ending March, 1997 :

Pension from Government Rs. 12,000

Salary from Company Rs. 18,000

Furnished rent-free bungalow provided by the company. It was formerly let out at Rs. 500 per month. Cost of furnishing is Rs. 15,000.

Entertainment allowance from the company at Rs. 250 per month.

Profit from business Rs. 25,000.

Dividends from Indian companies (gross) Rs. 8,000.

Interest from Government Securities Rs. 3,500.

He had taken a loan of Rs. 50,000, out of which Rs. 25,000 was invested in shares and the balance in Government securities. Interest for one year is payable on this loan @ 15% per annum.

He purchased a house for his residence in the year 1970 for Rs. 20,000. Its market value went up to Rs. 25,000 in 1980 but dropped down to Rs. 15,000 on 1.4.1981 [C.I.I.: 100]. It was sold off for Rs. 62,800 on 1.8.1996 [C.I.I.: 305].

He made a donation of Rs. 7,500 to a university.

Compute his total income for the assessment year and indicate the amount on which he is entitled to a rebate of income tax. *[M.Com. Kanpur]*

[**Hints :** Salary income Rs. 24,400. Business profit Rs. 25,000. Capital Gain Rs. 1,800, other sources Rs. 4,000; G.T.I. Rs. 55,200. Deduction u/s 80L Rs. 4,000 and u/s 80G Rs. 2,470. Total income Rs. 48,730 G. Taxable I for 80 G (55,200 – (4,000 + 1,800)]

Problem 31. Given below is the Income and Expenditure Account of Mr. Parkash C. Tandon, a lawyer.

Income and Expenditure Account

	Rs.		Rs.
To Household Expenses	7,000	By Legal fees	30,000
,, Office Expenses	5,000	,, Special Commission from profession	5,000
,, Donation to N.D.F.			

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(set up by State Government)	1,500	,, Gains on race course	2,000
,, Charity	400	,, Dividends on shares (Gross)	2,000
,, Loss on shares sold (Long-Term)	1,300	,, Profit on sale of Govt. Securities (Long-Term)	1,000
,, Income-tax	600	,, Share of Profit in a firm assessed as firm	4,400
,, Share of loss in a firm assessed as AOP	700	,, Interest on advances	500
,, Gratuity to one of his disabled clerks	500	,, Present from a client	600
,, Net income	35,600	,, Bank interest	500
		,, Interest on National Relief Bonds	5,400
		,, Director's fees	500
		,, Co-operative Society (Dividend)	700
	52,600		52,600

You are required to compute his total income.

[**Hints :** Professional Income Rs. 30,600, share from firm assessed as firm—Exempted, Capital Loss C/F Rs. 300; Other sources Rs. 4,200, G.T.I. Rs. 34,800. Deduction u/s 80L Rs. 3,200, 80G Rs. 750 Total Income 30,850]

Problem 32. The following is the Profit and Loss Account of a trader for the year ending 31st March :

	Rs.		Rs.
Office Salaries	10,000	Gross Profits	25,000
Rent	2,000	Rent of house let	4,800
Discount	1,000	Interest on Govt. Securities (Gross)	3,000
Commission	600		
Interest on loan	1,600		
Office Expenses	4,000		
Bad debts	500		
Charity	150		
Bad debts Reserve	2,000		
Insurance of property to tenants	90		
Embezzlement of cash by an employee	1,000		
Local Taxes	560		
Net Profit	9,300		
	32,800		32,800

The following additional information is also available :

(i) Interest on loan includes a sum of Rs. 600 paid to his wife on a loan taken from her.

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(*ii*) Office expenses included a sum of Rs. 200 spent by him as entertainment expenses on customers.

(*iii*) The assessee is also the owner of another house in which he is living. The municipal value of the house is Rs. 6,000 p.a.

(*iv*) Interest on loan includes interest of Rs. 700 paid to a non-resident who does not pay tax in India.

(*v*) Local taxes are in relation to the self-occupied house.

Compute the taxable income of the trader.

[**Hints :** Business Income Rs. 5,000, Income from House Property; Let out Rs. 3,750, Self-occupied Nil; Income from Other Sources Rs. 3,000; G.T.I. 11,750. Deduction u/s 80L Rs. 3,000. Total Income Rs. 8,750.]

Problem 33. Mr. S.B. Sharma, solicitor, prepared following income and expenditure account for the year ended 31st March.

	Rs.		Rs.
To office expenses	13,000	By Professional fees	1,25,000
,, Purchase of ornaments for his wife	9,000	,, Ground Rent	4,000
,, Household Expenses	36,000	,, Director's Fees	10,000
,, Wedding Expenses of his daughter	25,000	,, Interest on Govt. Securities	16,000
,, Life Insurance Premium on his life	7,000	,, Gifts on the occasion of daughter's marriage	18,000
,, School and College fees of his children	4,000		
,, Net loss on shares sold (Short-term)	10,000		
,, Charity	5,000		
,, Balance being Excess of Income over Expenditure	64,000		
	1,73,000		1,73,000

He lives in a bungalow which belongs to him. Its valuation as per municipal bill is Rs. 11,800 p.a. Expenses on this bungalow were : Ground Rent Rs. 800 and Fire Insurance Rs. 800.

From the above particulars, compute his total income.

[**Hints :** Income from self-occupied house—Nil: Professional Income—Rs. 1,12,000. Capital Loss Rs. 10,000 to be C/F Income from other sources Rs. 30,000; G.T.I. Rs. 1,42,000 Deduction u/s 80L Rs. 12,000. Total Income Rs. 1,30,000, Q.A. for rebate of tax u/s 88 Rs. 7,000]

Problem 34. Prof. Aziz Ahmed, an economist in a factory, gives the following information to you. Compute his total income for the current assessment year :

(*a*) Net Salary received Rs. 35,972; Income-tax deducted at source Rs. 4,000; Contributed to recognised provident fund Rs. 6,000 and equal amount being contributed by the employer company and professional tax deducted at source Rs. 528.

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(*b*) Received:

(*i*) in respect of interest on fixed deposit in a bank made on 10th December 1993, Rs. 4,000;

(*ii*) Rs. 300 being interest in post office savings bank account;

(*iii*) Rs. 2,700 as interest on Government Securities (net);

(*iv*) Rs. 2,300 as interest on Government Bonds (gross);

(*v*) Rs. 1,250 from Provident Fund account as interest calculated at the rate of 9% per annum; and

(*vi*) Received dividend (gross) amounting to Rs. 600.

(*c*) He owns a motor car which is used by him for purposes of his employment also.

(*d*) Amount disbursed during the year :

(*i*) Rs. 4,000 on a policy of Rs. 25,000;

(*ii*) Donation to National Defence Fund Rs. 1,000.

He pays Rs. 200 to an income-tax practitioner for advice in tax matters. He took a loan of Rs. 3,000 last year to clear up his income-tax dues and pays Rs. 500 as interest on it. *[Punjab, B.Com.]*

[**Hints :** Salary Rs. 46,500; Salary Income Rs. 31,372; Other sources Rs. 9,900; G.T.I. Rs. 41,272; Deductions u/s 80 G Rs. 500, 80L Rs. 9,900; Total Income Rs. 30,872; Q.A. for rebate of tax u/s 88 Rs. 10,000]

Problem 35. For the assessment year 1997-98 the following particulars of income have been obtained in the case of Mr. Bheemayya :

	Rs.
Income from house property (computed)	15,000
Profit from cloth business	8,000
Share of Profits from Gajanan Stores	2,000
Speculation income	3,000
Capital gains from short-term capital assets	3,000
Capital gains from long-term capital assets	9,000

The following losses have been brought forward from the preceding year:

(*a*)	loss from oil business discontinued during the earlier previous year	8,000
(*b*)	Share of loss from Gajanan Stores	5,000
(*c*)	Speculation loss	6,000
(*d*)	Loss under the head, Capital Gain's from Short-term capital assets	4,000
	From long-term capital assets	7,000

Compute the total income and indicate the amount of losses to be carried forward.

[**Hints :** House Property Income Rs. 15,000; Business profit Rs. 5,000; speculation loss still to be C/F Rs. 3,000; Capital Gains Rs. 1,000; G.T.I. Rs. 21,000; Loss of oil business cannot be C/F as the business was discontinued]

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TOTAL INCOME OF H.U.F.'S

Problem 36. Atma Ram and Sons is a H.U.F. of which P is the karta. The family consists of karta and his three brothers—Q, R, S as coparceners. The family and the coparceners have the following incomes :

(*i*) Salary of R as manager of a company Rs. 18,000.

(*ii*) Interest on Securities :

(*a*) In the name of Q (investment made out of his salary) Rs. 4,200.

(*b*) In the name of all the coparceners (investment made out of family funds) Rs. 2,900.

(*iii*) House Property:

(*a*) Ancestral house Rs. 12,000 (Self-occupied).

(*b*) In the name of P (brought in 1954 out of family funds Rs. 7,500. (Let out).

(*iv*) Business :

(*a*) Family business income Rs. 35,000.

(*b*) Half-share of income in a firm assessed as AOP in which P is a partner in a representative capacity Rs. 3,600.

(*c*) Income from profession as a lawyer of R, Rs. 9,500.

(*v*) Dividend from shares :

(*a*) In the name of P bought out of family funds (gross) Rs. 3,000.

(*b*) In the name of P's wife bought out of her stridhan Rs. 1,200.

Compute the total income of the family.

[P.U., Pbi. U., B.Com. & Kanpur, M.Com.]

[**Hints :** House property income Rs. 6,000, Business Income Rs. 38,600. Other Sources Rs. 5,900. Gross Total Income Rs. 50,500. Deduction u/s 80 L Rs. 3,000. Total Income Rs. 47,500. Income from Investments of Q: from profession of lawyer and dividend of P's wife are their individual incomes]

Problem 37. A Hindu Undivided family carrying on business in gold, silver, money-lending, brokerage, shares and securities dealings showed the following particulars in a statement filed for the previous year :

	Rs.		Rs.
Loss in silver	70,000	Profit in gold	2,00,000
Loss in sale of securities	50,000	Income from money lending business	40,000
Loss in share dealings	30,000	Income from brokerage	2,00,000
Legal charges	10,000	Interest on securities (Gross)	60,000
Bad debts	20,000		
Establishment charges	50,000		
Net Profit	2,70,000		
	5,00,000		5,00,000

On inquiry and examination of account books the following further information was obtained :

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(*a*) A loss of Rs. 60,000 in hedging contract and a loss of Rs. 40,000 in speculation were found debited to Silver Account.

(*b*) Legal charges included expenses of Rs. 1,000 incurred in a criminal case connected with alleged purchase of smuggled gold.

(*c*) Bad debts includes loss of cash of Rs. 5,000 by theft during night from safe box of the business premises and Rs. 10,000 as an irrecoverable loan given without interest to his brother-in-law, whose business failed.

(*d*) Establishment charges included salary of Rs. 5,000 paid to the son of the Karta who actually worked in the business and claimed Rs. 32,000 for purchase of a motor cycle on 1st July, 1996 to enable him to attend business work.

Compute the total income of the H.U.F. for the assessment year 1997-98.

[Punjab, B.Com., April 1987]

[**Hints :** Hedging loss is business loss: Speculation loss of Rs. 40,000 will be C/F, Legal charges of criminal case are not allowed: Bad debt of a loan without interest not allowed; Salary to son of Karta allowed; Motor cycle capital exp. Depreciation on Motor cycle @ 25% Total Income 3,45,000]

Problem 38. A is the Karta of a Mitakshara Hindu undivided family; B and C are his two adult sons. You are to determine the total income of the H.U.F. The relevant data are given below :

1. The H.U.F. runs a business in hosiery goods, the net income returned from it is Rs. 11,000. This figure was arrived at after charging Rs. 8,000 as salary payable to B and C, who help in running the business.
2. Rejecting the trading account, you hold that Rs. 20,000 has to be added to the gross profits.
3. No satisfactory explanation can be furnished by the assessee regarding a deposit of Rs. 38,000 made in the name of one F in the books of the family's business.
4. The H.U.F. has been holding for the past ten years 4,000 shares, out of 20,000 shares issued by an Indian Public Limited Company. The shares owned by the H.U.F. are held in the name of A, who was made a managing director of the company during the relevant accounting year and received Rs. 12,000 as director's remuneration and Rs. 1,200 as director's fees.
5. A dividend of Rs. 7,000 (Before deduction of Rs. 1,400 as tax) has been received on the shares held in the name of the Karta referred to in (4) above.
6. On 31.5.1996 [C.I.I. 305] one of the house properties (shop) owned by the H.U.F. since 1981 was sold for Rs. 62,400. Its fair market value as on 1.4.1981 [C.I.I. 100] is estimated to have been Rs. 20,000.
7. The H.U.F. has paid Rs. 10,000 as life insurance premium on policies taken for B and C. It has paid further Rs. 20,000 for the purchase of National Savings Certificates (VIII issue) in the name of B.

[**Hints :** Business Income Rs. 31,000; Capital Gains: Shop 1,400; other sources Rs. 58,200; G.T.I. Rs. 90,600; Deduction u/s 80L Rs. 7,000; Total Income Rs. 83,600 Q.A. for rebate of tax u/s 88 Rs. 30,000. Karta became director because of shares held by the H.U.F. and so director's fees and managing director's remuneration shall be H.U.F. income]

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Problem 39. A Hindu undivided family carrying on a trade in provisions declared an income of Rs. 23,000 in its return of income made for the assessment year 1997-98. The following particulars are available :

1. Salaries of Rs. 4,800 and Rs. 1,200 respectively paid to the Karta and Karta's wife for service rendered are claimed as expense.
2. A gift of Rs. 10,000 had been made by the Karta in an earlier year to his minor unmarried daughter out of the family funds. The amount was deposited with a bank in her name and it earned interest of Rs. 750 in the year.
3. The declared income included Rs. 3,200 being share of profit in a firm assessed as AOP HJK. In arriving at this amount, the H.U.F. had deducted a sum of Rs. 1,200 for charges incurred by the Karta in maintaining an establishment to look after his interests in the firm and another sum of Rs. 600 being interest paid by the Karta on moneys borrowed by him and advanced to the firm as a loan.
4. The Karta's wife is also a partner in the firm assessed as firm HJK. Her share of income for the assessment year 1997-98 was Rs. 6,000 and it was not included in the declared income of Rs. 23,000.
5. A sum of Rs. 20,000 appeared in the accounts in favour of Mr. X. On enquiry the I.T.O. found that Mr. X was employed on a petty salary and had little means. All the same, Mr. X affirmed on oath that he had advanced the loan.
6. A sum of Rs. 15,000 appeared in the accounts as a credit in favour of the Karta's wife and the narration in the entry was that amount was the sale price for her old ornaments. A reputed jeweller's bill was produced to prove the sale. The purchase of the ornaments was not proved.
7. The Balance Sheet showed a difference of Rs. 395, being the excess of the total of the Capital and Liabilities side over the total of the Property and Assets side.
8. The family had advanced a loan of Rs. 10,000 on a promissory note at 9% interest in the year 1994. The debtor did not make any payment. The family obtained from the debtor in the year ended 31.3.97 a fresh promissory note for Rs. 12,700 which included interest for the three years. It was contented that the amount of Rs. 2,700 representing interest was not assessable for the year.

Compute the income of the H.U.F.

[Hints : HUF's total income Rs. 23,000 + Unexplained cash credit Rs. 20,000 + cash credit of jewellery Rs. 15,000 + Interest for the year Rs. 900 = Rs. 58,900 (Arrears of interest presumed to be taxed when due). Gift is allowed, hence interest is tax-free. Wife's share from firm is not to be included in HUF income u/s 64 (1). Excess of the total of liabilities side of Balance sheet over its assets side is not income]

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TOTAL INCOME OF PFAF AND PFAOP

Problem 40. Ambika, Balika and Capalika are equal partners in a firm. The firm has earned from business Rs. 30,000 for the year ended 31st March 1997. Besides the firm also received Rs. 21,000 as rent from a let out house property during the year. Local taxes and repair charges of the house are Rs. 1,000 and Rs. 5,000 respectively.

The income of the business has been arrived at after debiting the following items :

1. Salary to Mr. Capalika Rs. 5,000.
2. Rs. 3,000 paid as Rent to Mr. Balika for the building in which the office of the firm is situated.
3. Depreciation on Furniture Rs. 1,500 which includes Rs. 500 paid towards the purchase value of a table.
4. General expenses Rs. 8,000 which include interest on capital of the partners Rs. 600 each.
5. Reserve for Bad debts Rs. 3,000.

Compute the total income of the firm (treated as A.O.P.) for the Assessment year 1997-98 and allocate it amongst the partners.

[**Hints :** Firm's (treated as A.O.P) Business Income Rs. 40,250; HP Rs. 16,000; Total Income Rs. 56,250; Ambika's share Rs. 17,083; Balika's share Rs. 17,083 Capalika's share Rs. 22,084]

Problem 41. XYZ are three partners of a firm sharing profit and losses in the ratio of 2 : 3 : 5. The firm is assessed as 'PFAOP'. The profit and loss account of the firm for year ending March 31, 1997 is as follows :

	Rs.		Rs.
Cost of goods sold	1,14,000	Sales	3,00,000
Interest to partners :		Short term capital gain	1,30,000
X	6,000		
Y	16,000		
Z	12,000		
Salary to partners :			
X	45,000		
Z	19,000		
Other expenses	40,000		
Net profit	1,78,000		
	4,30,000		4,30,000

Other information :

1. The firm gives a donation of Rs. 23,000 to a public charitable trust (not debited to P/L A/c) which is eligible u/s 80G.
2. Out of other expenses Rs. 14,000 is not deductible by virtue of section 43B.

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Other income of the partners are given below :

	Amount Rs.	Nature of Income	Deductions u/s 80D to 80U	PPF contribution Rs.
X	36,000	Bank interest	Rs. 3,000 medical insurance premia	4,000
Y	30,000	Dividend from Indian Co.	—	2,000
Z	32,000	Interest on company deposit	Rs. 4,000 medical insurance premium	1,000

Find out the tax liability of the firm and partners for the assessment year 1997-98. *(B.Com., P.U. 1995)*

[**Hints :** AOP's total income Rs. 2,78,500; AOP's Tax Rs. 84,400 Partner X's Total income Rs, 1,08,100 rebate u/s 86 Rs. 14,044 u/s 88 Rs. 800 Net Tax Rs. 2,586; PartnerY's Total income Rs. 85,150 Rebate u/s 86 Rs. 8,687 u/s 88 Rs. 400. Net tax Rs. 1,458; Partner Z's Total income Rs. 1,49,250 Rebate u/s 86 Rs. 26,565 u/s 88 Rs. 200 Net tax Rs. 5,935]

Problem 42. A firm's profit and loss account for the year ending on 31st March 1997 showed a net profit of Rs. 3,35,200 after debiting the following amounts :

		Rs.
(*a*)	Salary paid to Z	8,000
(*b*)	Rent paid to X for building in which the firm's office was situated	18,000
(*c*)	Interest on Capital @ 15% paid to X	2,000
	to Y	4,000
	to Z	6,000
(*d*)	Commission on sale paid to Y	20,000
(*e*)	Expenses on current repairs of the business premises belonging to Partner X	2,000
(*f*)	Donations to approved bodies	10,000

The net profit of Rs. 3,35,200 included Rs. 19,200 from interest on Government securities (after deduction of tax at source Rs. 4,800).

Compute the total income of the firm. The firm has submitted the deed alongwith return of assessment year 1997-98. It provides for payment of salary of Rs. 8,000 to Z and Commission on sale to Y of Rs. 8,000. It does not provide for payment of any interest on capital.

[**Hints :** Firm's Income Rs. 3,71,000]

Problem 43. Ajay, Biren and Charu are active partners in a firm assessed as AOP of cloth dealers. The firm's profit and loss account for the year ended 31st March, 1997 is appended below. Compute the total income of the firm for income-tax purposes and allocate the same amongst the partners.

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	Rs.		Rs.
To Salaries	16,500	By Gross Profit	1,20,000
,, Rent, Rates etc.	6,000	By Interest on Partner's Drawings :	
,, Income-tax	3,250		
,, Advertisement	1,500		
,, Postage and Telegram	1,300		
,, Reserve for Bad Debts	1,750		
,, Fire Insurance Premium	1,200		
,, Salary paid to partners:			
Ajay 6,000		Ajay 1,200	
Biren 4,800		Biren 850	
Charu 3,600		Charu 450	
	14,400		2,500
,, Interest on Capital :			
Ajay 1,200			
Biren 2,400			
Charu 3,000			
	6,600		
,, Net Profit:			
Ajay 50% 35,000			
Biren 30% 21,000			
Charu 20% 14,000			
	70,000		
Total	1,22,500	Total	1,22,500

[Adapted from I.C.W.A. Final]

[**Hints :** Firm's (treated as AOP) Business and Total Income Rs. 93,500. Ajay's share Rs. 43,500, Biren's share Rs. 28,850, Charu's share Rs. 21,150 Interest on Partner's drawings is income of the firm]

Problem 44. Compute the total income of the firm consisting of A B C, [C is not a working partner] having interest in the ratio 1/2, 1/4, 1/4, respectively from the following particulars during the year :

(*a*) Net profit before depreciation on building and furniture Rs. 56,000.

(*b*) Allowable depreciation for the year is Rs. 13,700.

(*c*) Profit and Loss A/c shows the undernoted expenses :

(*i*) Partner's salary: A Rs. 10,000; B Rs. 6,000 and C Rs. 21,000.

(*ii*) Rent and Taxes A/c Rs. 4,500 includes rent paid to A for office Rs. 2,400; Municipal taxes paid Rs. 1,500 for a house owned and used by B and income-tax payment of Rs. 600.

(*d*) Opening stock and closing stock stand at Rs. 38,000 and Rs. 95,000 respectively. It is the practice to undervalue stocks at 5%.

(*e*) A penalty of Rs. 2,000 for dealing in contraband goods has been debited in Sundry Expenses A/c. *[Nagpur, M.Com.]*

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The firm has submitted certified copy of deed along with return as it provides for payment of salary to A Rs. 10,000 and B Rs. 6,000.

[**Hints :** Difference of Rs. 3,000 due to undervaluation of stock is to be added back. Total Income Rs. 70,400]

Problem 45. X, Y and Mrs. Y are partners in a firm sharing profits and losses equally. For the previous year 1996-97 the net profit as per profit and loss account was Rs. 1,10,000. The following points were noticed on scrutiny of the account books.

(*i*) Salary of Rs. 90,000 was paid to partner X who is a working partner.

(*ii*) Rent of Rs. 9,000 was paid to Mr. Y as rent for the property used by the firm for its business. It was stated that the property was constructed in 1984 out of money gifted by her husband.

(*iii*) Interest of Rs. 9,000 each was credited to the capital accounts of X, Y and Mrs. Y @ 20% p.a. It was stated that the capital invested by Mrs. Y was gifted to her by her father.

(*iv*) Expenses debited include Rs. 500 for partnership deed expenses.

(*v*) It was claimed that Rs. 10,000 credited to the profit and loss account should be deducted as it represented receipt of capital nature. It was stated that the amount had been received from textile mill as damages for failure to deliver goods as per contract.

Compute the total income of the firm in which X, Y and Mrs. Y are partners. The firm has submitted a certified copy of deed along with return. It provides for payment of salary to X @ Rs. 7,500/- p.m. and Interest on capital @ 20% p.a.

[**Hints :** Interest of Rs. 2,700 disallowed. Firm's income Rs. 1,13,200; X's income P & G Rs. 98,100 Mrs. Y's income P & G Rs. 8,100 Mr. Y's income HP Rs. 7,200 P & G Rs. 8,100]

Problem 46. (1) ABCD is a firm of four partners constituted under the Instrument of partnership dated first January, 1994 but it was not submitted along with return. The assessment for 1996-97 is pending. Profits and losses are shared equally after providing for salary, commission and interest as per the agreement.

2. The profit of the firm after paying Rs. 6,000 as salary to partner 'A', Rs. 3,000 as interest to 'B' and Rs. 5,000 as commission to partner 'C', is Rs. 5,000. The Depreciation and Investment Allowance have been claimed in the accounts correctly.

3. Partner 'A' is a director in 'Z' Co. (P) Ltd., holding 40 per cent of its ordinary share capital. According to the Company's Balance Sheet as on 30th April, 1995 its paid-up capital was Rs. 50,000 and it had an equal amount of accumulated profits. On 1st May, 1996 he took a loan of Rs. 4,000 from the company. It has not so far been repaid. His other income consists of share of income from a Hindu Undivided Family of which he is a coparcener, Rs. 1,500. The other income of 'B' consists of dividend income from M/s 'Y' Ltd., Rs. 1,000, debenture interest from M/s 'Y' Ltd., Rs. 250, and share of Income from an A.O.P. of four partners sharing profits and losses equally Rs. 8,000. He is also a shareholder in M/s Z Co. (P) Ltd. holding 5 per cent of the ordinary issued share capital. During the year he received a loan on 1st May, 1996 of Rs. 500 from the company. The other income of 'C' is only house property income of Rs. 750. During the year on 1.5.1996 he won a treble event on the race course and prize was Rs. 25,000. Out of savings of earlier years

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he had purchased a house property in the name of his wife the computed income of which is Rs. 1,200. Mr. 'D' is a non-resident and has no other Indian income.

Compute the total income of the firm and the partners for assessment year 1997-98.

[**Hints :** Firm's (treated as AOP) total income Rs. 19,000; A's share Rs. 7,250; B's share Rs. 4,250; C's share Rs. 6,250 and D's share Rs. 1,250 A's Total Income Rs. 7,250 [Loan of Rs. 4,000 is treated as dividend u/s 2(22)]; B's Total Income Rs. 12,500; C's Total Income Rs. 30,700, D's Total Income Rs. 1,250 only]

TOTAL INCOME OF COMPANIES

Problem 47. Given below is the Profit and Loss Account of Modern Co. Ltd.

	Rs.
To Opening stock	5,50,000
,, Purchases	55,60,000
,, Railway, Freight, Octroi etc.	6,00,000
,, Salaries	4,50,000
,, Director's Fees	6,000
,, Audit Fees	5,000
,, Legal Expenses	50,000
,, Repairs to Building & Machinery	14,000
,, Welfare Expenses	10,000
,, General Charges	25,000
,, Interest paid	2,50,000
,, Reserve for B/D	5,000
,, Depreciation	10,000
,, Managing Agent's Remuneration	30,000
,, Debenture Sinking Fund	25,000
,, Proposed Dividend	6,00,000
,, Balance carried to Balance Sheet	1,66,000

Compute Company's total income after taking into account the following information:

1. Rs. 5,000 on account of a liability foregone by a creditor, to whom that sum was due by way of commission charged by the company in the revenue account of the preceding year have been carried to a special reserve.
2. General charges include:
   (*i*) Rs. 1,000 Insurance of staff quarters.
   (*ii*) Rs. 3,000 Repairs of staff quarters.
   (*iii*) Rs. 3,000 Municipal taxes of staff quarters.
   (*iv*) Rs. 5,000 Donations.
3. Welfare expenses include Rs. 7,000 for installing water cooler machine for workers.
4. Legal expenses include Rs. 3,500 paid for the prosecution of Managing agents for smuggling to Pakistan.

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5. Repairs to building include Rs. 10,000, being cost of additions to business premises.
6. Depreciation is Rs. 20,000. *[Nagpur M.Com.]*

[**Hints :** G.T.I. Rs. 15,16,500; Deduction u/s 80G Rs. 2,500. Total Income Rs. 15,14,000. Allowable Depreciation includes depreciation on water cooler machine and extension in business building, liability foregone is taxable income of that year]

Problem 48. From the following information, compute the company's Total Income.

P & L A/c

	Rs.		Rs.
Opening stock	52,400	Sales of Sugar	11,52,500
Cane purchased	4,75,200	Transfer Fees	300
Manufacturing Expenses	2,59,000	Rent of agricultural lands	1,000
Salaries and wages	45,500		
General charges	8,500		
Commission and Brokerage	36,400		
Interest on loan	8,500		
Director's fees	1,200		
Income-tax	35,800		
Reserve for Bad Debts	19,500		
Depreciation	69,000		
Provision for dividends	30,000		
Net Profit	1,12,800		
	11,53,800		11,53,800

(*a*) General Charges include :
- (*i*) Rs. 1,000 as donation to hospital.
- (*ii*) Rs. 1,000 subscription to sugar syndicate.
- (*iii*) Rs. 2,600 commission to broker for arranging a loan for the company.
- (*iv*) Rs. 2,000 paid to a director for a trip to Hawaii to study modern methods in confectionery manufacture.

(*b*) The actual bad debts amounted to Rs. 6,000.

(*c*) Depreciation is Rs. 72,000 *[Nagpur University, M.Com.]*

[**Hints :** Business Profit—Rs. 1,90,800; G.T.I. Rs. 1,90,500; Deduction u/s 80G—Rs. 500; Total Income—Rs. 1,90,000; Expenses on Hawaii tour belong to a separate business and hence disallowed. Subscription to sugar syndicate is an allowable expenditure]

Problem 49. The following is the Trading and Profit and Loss Account of a Limited Company for the year ended 31st March, 1997. The company is dealing in Textiles.

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Trading Account

	Rs.		Rs.
To Opening stock	75,000	By Sales	13,50,000
,, Purchases	10,00,000	,, Closing stock	50,000
,, Freight	7,000		
,, Customs	50,000		
,, Gross Profit	2,68,000		
	14,00,000		14,00,000

Profit and Loss Account

	Rs.		Rs.
To Salaries	60,000	By Gross Profit	2,68,000
,, Rent	12,000	,, Interest (Gross)	10,000
,, Rates and Taxes	10,000	,, Dividend (Gross)	6,000
,, Interest	50,000		
,, Bad debts Reserve	1,000		
,, Depreciation	8,000		
,, Interim Dividend paid	20,000		
,, Misc. Expenses	60,000		
,, Net Profit	63,000		
	2,84,000		2,84,000

The following facts are available from the records :

(*a*) Closing stock has been valued at market rates which was less than the cost by 10%. Valuation of closing stock in the preceding year has been at cost.

(*b*) Purchases include Rs. 1,00,000 advanced to a Textile Mill against supply of cloth agreed to be delivered in April 1997.

(*c*) A penalty of Rs. 30,000 was paid to the Customs Dept. for violation of import quota rules. This is included in the Trading Account.

(*d*) Salaries included Rs. 36,000 paid to the Managing Director. Of this Rs. 24,000 represented salary and Rs. 12,000 paid as Motor Car Advance.

(*e*) Rates and Taxes included Rs. 3,000 paid as advance income-tax.

(*f*) Interest payment of Rs. 50,000 is towards unpaid balance of purchase price to the vender from whom the business was purchased by the company as a going concern.

(*g*) Miscellaneous expenses include Rs. 30,000 paid as bonus to staff. This bonus relates to the year 1994-95 but was settled by an agreement in February 1997.

(*h*) Dividend has been received from an Indian Company producing cement.

Compute the total income of the company for assessment year 1997-98.

[Nagpur M.Com.]

[Hints : Difference due to undervaluation of stock Rs. 5,559 to be added back. Business Income 2,68,556, other sources 16,000, G.T.I. 2,84,556. Deduction u/s 80M not allowed; Total Income 2,84,556]

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Problem 50. X Ltd. a new company began manufacturing tools on 1st September 1994. Its Balance Sheet on 31st March, 1997 shows:

	Rs.			Rs.
Authorised Capital 50,000, Shares of Rs. 10 each	5,00,000	Land		45,000
		Factory Buildings		50,000
Subscribed Capital 30,000 Shares fully paid	3,00,000	Plant and Machinery	2,00,000	
		Less : Dep.	50,000	1,50,000
Profit and Loss Account	36,565			
Trade Creditors	39,700			
Expenses Owing	3,200	Furniture		15,000
		Stock		13,000
		Debtors	79,000	
		Less : Provision for Bad Debts	3,935	75,065
		Cash at bank		30,000
		Cash in hand		1,400
	3,79,465			3,79,465

Debits in the Profit and Loss Account include, *inter alia*, the following:

(*i*) Rs. 2,800 expenses for registration of the trade mark of Factory.

(*ii*) Rs. 19,000 tour expenses of the managing director of the company, who went to the U.S.A. to study the set-up and working of tool manufacturing concerns.

(*iii*) Rs. 5,400 expenses on sending the son of managing director to the U.S.A. for training in tool-manufacturing, the term of agreement being that on return from U.S.A., with degree qualification in tool manufacturing, he would serve the company for three years on a monthly salary of Rs. 1,500 as against Rs. 2,500 being paid at present to a foreign expert employed by the company.

(*iv*) Rs. 6,000 commission paid to underwriters of the shares of the company.

Calculate the total income of the company for the assessment year 1997-98.

[Adapted from M.Com. Kanpur]

[Hints : 1/14th of registration of Trade Mark expenses allowed. Tour expenses of the Managing Director presumed to be preliminary expenses and 1/10th allowed. Rs. 5,400 spent on sending the son of Managing Director to U.S.A. allowed being in the company's long-term interest. 1/10 underwriter's commission allowed.

Business Income Rs. 59,100; Depreciation allowed Rs. 56,500 Deduction u/s 80IA @ 30% of Rs. 59,100 *i.e.*, Rs. 17,930 Total Income Rs. 41,370]

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3 OBJECTIVE TYPE QUESTIONS

These questions can carry upto 1% marks in a question paper.

P—1

Reproduce the correct answer:

(*i*) Income from rent of agricultural lands is
- (*a*) Agricultural Income
- (*b*) Business Income
- (*c*) Casual Income.

(*ii*) Income from tea cultivation and manufacturing of tea business has to be divided in two parts :
- (*a*) 40% is Agricultural Income
- (*b*) 50% is Agricultural Income
- (*c*) 60% is Agricultural Income.

(*iii*) Integration of Agricultural Income and Non-Agricultural Income is not done in case of
- (*a*) Individuals
- (*b*) Partnership firm assessed as AOP
- (*c*) Companies.

(*iv*) Income of previous year (1.6.1996 to 31.3.97) is taxable in the assessment year.
- (*a*) 1997-98
- (*b*) 1996-97
- (*c*) 1995-96.

(*v*) Income from sale of household furniture is
- (*a*) Taxable Income
- (*b*) Exempted Income
- (*c*) Casual Income.

(*vi*) Share of income received by a member of H.U.F. out of H.U.F. income is
- (*a*) Taxable income u/s 66
- (*b*) Exempted income u/s 10(2)
- (*c*) Rebatable income u/s 86.

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(*vii*) No integration of agricultural income with non-agricultural income if agricultural income is below :
- (*a*) Rs. 40,000
- (*b*) Rs. 600
- (*c*) Rs. 18,000.

(*viii*) Share of income received from an A.O.P. (whose income is liable to tax at rates applicable to an individual) is entitled to rebate at
- (*a*) $27^1/_2\%$
- (*b*) Nil
- (*c*) Average rate.

(*ix*) In case of Hindu undivided family (which has at least one member whose individual income exceeds Rs. 40,000) the exempted limit of income for assessment year 1997-98 is :
- (*a*) Rs. 40,000
- (*b*) Rs. 18,000
- (*c*) Rs. 35,000.

Solution

(*i*) (*a*) Agricultural income, (*ii*) (*b*) 60% is Agricultural income, (*iii*) (*c*) Companies, (*iv*) (*a*) 1997-98, (*v*) (*b*) Exempted income, (*vi*) (*b*) Exempted u/s 10 (2), (*vii*) (*b*) Rs. 600, (*viii*) (*c*) Average rate, (*ix*) (*b*) Rs. 40,000.

P—2

(A) *Fill up the blanks. Write the complete sentences in the answer book underline the filled up parts :*

1. The income derived from land can either be in the shape of rent or in the shape of.....received by performing certain agricultural operations personally.
2. Section 14 of Income-tax Act, 1961 provides for the computation of total income of an assessee under.....
3. For a payment to be considered under the head salaries, the relationship of.....and.....must exist between the payer and receiver of the salary.
4. Assets transferred after a period of 36 months is called.....asset.
5. The computation of a firm's income is done first as income is computed under the head.....

(B) *State whether the following statements are true or false*:

1. Perquisite can be only in monetary form. F
2. For assessment year 1997-98, assessee with a total income upto Rs. 40,000 p.a. need not pay tax. T
3. Provident Funds governed under Public Provident Fund Scheme are called Recognised Provident Fund. F
4. Savings in the form of cumulative time deposits in a Post Office qualify for rebate for tax purposes. T
5. Any amount received by a government servant as commutation of pension is fully tax free. T

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Solution

(A) (1) Revenue, (2) Five heads, (3) Employer and employee, (4) Long-term capital, (5) Profit & Gains.

(B) (1) False, (2) True, (3) False, (4) True, (5) True.

P—3

(A) Choose the correct answer for each of the following from the given three suggestions and write it :

1. Standard deduction allowed to an assessee if a car is provided by his employer is
   (*a*) Rs. 1,000/- p.a.
   (*b*) To a maximum amount of Rs. 15,000/-
   (*c*) An amount at the discretion of the Assessing officer.
2. In respect of income from house property, the collection charges are allowed upto maximum of
   (*a*) The actual expenditure incurred
   (*b*) 6% of the annual value
   (*c*) NIL.
3. For any loss to be carried forward and set off against the income of a subsequent year the return of such loss must be filed :
   (*a*) Under section 139 (4)
   (*b*) Under section 140 (1)
   (*c*) Under section 144 (2).
4. If an assessee pays some interest on a loan borrowed to pay any tax due, he shall be entitled to claim a deduction of
   (*a*) Full amount of such interest paid
   (*b*) 50% of such interest paid
   (*c*) Not entitled to any such deduction.

(B) Match the following :

List A	List B
(*i*) House-rent allowance	(*a*) Taxable income
(*ii*) Casual income	(*b*) A perquisite
(*iii*) Collection charges on interest on securities	(*c*) A deduction from income
(*iv*) Best judgement assessment	(*d*) A step taken by tax authorities
(*v*) Capital gain	(*e*) An exempted income
	(*f*) Partly taxable allowance.

Solution

(A) (1) (*b*) Rs. 15,000 p.a., (2) (*c*) NIL, (3) (*a*) Under section 139, (4) (*c*) Not entitled to any deduction.

(B) (*i*) and (*f*), (*ii*) and (*e*), (*iii*) and (*c*), (*iv*) and (*d*), (*v*) and (*c*).

P—4

(A) *Reproduce, in full, each of the sentences by filling up the blanks :*

(*a*) Interest received on company debentures is assessable under the head

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(*b*) Preliminary expenses incurred by an Indian company are allowed to be amortised equally in.....years.

(*c*) When the previous year of an assessee not having business income ends on 31st March, the last date for filling the return of income is.....

(*d*) Deduction for interest on loan taken for construction of self-occupied house is allowed up to actual or Rs.....w.e. is less.

(B) *State whether following statements are true or false*:

(*a*) The entire interest credited to the Recognised Provident Fund Account of an employee is tax-free.

(*b*) Income from property for a year cannot be in the negative.

(*c*) A separate schedule of tax rates is prescribed in respect of capital gains for individual assessees.

(*d*) Commission paid to the bank for the collection of dividend warrants is deductible while computing the income from dividends.

[C.A. Inter, May 1984]

Solution

(A) (*a*) Interest received on company debentures is assessable under the head "Income from other sources".

(*b*) Preliminary expenses incurred by an Indian company are allowed to be amortised equally in *ten* years.

(*c*) When the previous year of an assessee not having business income ends on 31st March, the last date for filing the return of income is *30th June next.*

(*d*) Deduction for interest on loan taken for construction of self-occupied house is allowed up to actual or Rs. 15,000 w.e. is less.

(B) (*a*) False (upto 12% Exempted), (*b*) False, (*c*) True, (*d*) True.

P—5

Reproduce the correct answer:

(*i*) Integration of agricultural and non-agricultural income of an individual shall be made during the assessment year 1997-98 only if the non-agricultural income exceeds :

(*a*) Rs. 40,000

(*b*) Rs. 15,000

(*c*) Rs. 600.

(*ii*) **An individual who wants to be resident of India u/s 6 (i)(a) must stay in India for at least**

(*a*) 182 days

(*b*) 365 days

(*c*) 730 days in 7 previous years.

(*iii*) **Salary paid by an Indian company to its employee working in one if its branches outside India is :**

(*a*) Salary accruing in India

(*b*) Salary deemed to accrue in India

(*c*) Salary accruing outside India.

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(*iv*) Compensation for cancellation by the government of a licence resulting in cessation of business is :
- (*a*) a casual receipt
- (*b*) a revenue receipt
- (*c*) a capital receipt.

(*v*) Any payment made to discharge a revenue liability. If refunded later on, shall be :
- (*a*) a revenue receipt
- (*b*) a capital receipt
- (*c*) a casual receipt.

(*vi*) Embezzlement of cash by a cashier is :
- (*a*) a revenue loss
- (*b*) a capital loss
- (*c*) a casual loss.

(*vii*) Dividend by an Indian company paid outside India is :
- (*a*) Income accruing in India
- (*b*) Income deemed to accrue in India
- (*c*) Income accruing outside India.

(*viii*) Income from transfer of capital asset situated outside India is taxable in case of an Indian resident as :
- (*a*) an income accruing in India
- (*b*) Income received in India
- (*c*) Income earned and received outside India.

(*ix*) Mr. B leaves India for the first time on 15.9.95 and comes back on 5.9.1996. His residential status for the previous year 1996-97 is :
- (*a*) a resident u/s 6(1)(*a*)
- (*b*) a resident u/s 6(1)(*b*)
- (*c*) a non-resident.

(*x*) Proceeds of benefit match received by a cricket player are :
- (*a*) a professional income
- (*b*) a casual income
- (*c*) an exempted income.

Solution

(*i*) (*a*) Rs. 40,000, (*ii*) (*a*) 182 days, (*iii*) (*c*) Salary accruing outside India, (*iv*) (*c*) Capital receipt, (*v*) (*a*) Revenue receipt, (*vi*) (*a*) Revenue loss, (*vii*) (*b*) Income deemed to accrue in India, (*viii*) (*c*) Income earned and received outside India, (*ix*) (*a*) Resident u/s 6(1)(*a*), (*x*) (*b*) a casual income.

P—6

(*i*) The income for the previous year (1st April 1996 to 31st March, 1997) is assessable for the assessment year :
- (*a*) 1995-96
- (*b*) 1996-97
- (*c*) 1997-98.

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(*ii*) Under the Income-tax Act, the incidence of taxation depends on :
- (*a*) the citizenship of the tax-payer

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(*b*) the age of the tax-payer
(*c*) the residential status of the tax-payer.

(*iii*) Dividends on shares held as stock-in-trade of an assessee's business should be included in his total income as
(*a*) income from business
(*b*) interest on securities
(*c*) income from other sources.

(*iv*) Income to the cultivator from commercial agricultural crops such as jute, cotton, groundnuts, sugarcane, etc. is treated as :
(*a*) business income
(*b*) agricultural income
(*c*) income from other sources.

(*v*) Standard deduction allowed in computation of income under the head 'Salaries' for the assessment year 1997-98 for female employees is
(*a*) $33^1/_3$% of salary subject to a maximum of Rs. 18,000
(*b*) 30% of salary subject to a maximum of Rs. 10,000
(*c*) 25% of salary without any limit.

(*vi*) Mr. Roy carrying on business as a chemist and a druggist and who spent Rs. 6,000, in respect of appeal proceedings before the Income-tax authorities, can claim :
(*a*) the whole of it as revenue expenditure
(*b*) Rs. 5,000 as a deduction from his Gross Total Income
(*c*) No deduction.

(*vii*) Unabsorbed depreciation can be carried forward for set off :
(*a*) for a period of four years only
(*b*) for a period of eight years only
(*c*) for an unlimited number of years.

(*viii*) Mr. Sarkar and Mrs. Sarkar are qualified Chartered Accountants and are carrying on profession as partners in the same professional firm assessed as firm.
(*a*) The share of income of both the partners will be clubbed under the provisions of Section 64
(*b*) The clubbing provisions of Section 64 will not apply to them
(*c*) The share income from the firm will be exempt from tax.

(*ix*) If a resident individual assessee spends Rs. 60,000 for developing export markets abroad in the accounting year relevant to assessment year 1997-98 he will be entitled to a deduction of :
(*a*) Rs. 60,000
(*b*) Rs. 80,000
(*c*) Rs. 30,000
(*d*) Rs. 40,000. *[C.A. Inter]*

Solution

(*i*) (*c*) 1997-98
(*ii*) (*c*) the residential status of the tax-payer
(*iii*) (*c*) income from other sources

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(*iv*) (*b*) agricultural income
(*v*) (*a*) $33^1/_3$% of salary subject to a maximum of Rs. 18,000
(*vi*) (*a*) As revenue expenditure
(*vii*) (*c*) for an unlimited number of years
(*viii*) (*c*) Share of income from firm will be exempted
(*ix*) (*a*) Rs. 60,000.

P—7

In each of the following sub-questions, out of the three alternatives, state which is most appropriate by reproducing it :

(*i*) A, an officer belonging to the Indian Foreign Service is posted at New York and for the financial year 1996-97 receives a salary of Rs. 54,000 from the Government of India. This sum will be:
(*a*) exempt from tax in India since it has been paid outside India.
(*b*) taxable in India since he is an Indian citizen and he has been paid for service rendered outside India.
(*c*) taxable only by the United States Government.

(*ii*) Mr. Singh is transferred to New Delhi and is paid a shifting allowance of Rs. 12,000 by his employer's out of which he spends Rs. 10,000 for shifting his family and personal effects. In this case :
(*a*) The whole of Rs. 12,000 is exempt from tax under Section 10(14)
(*b*) Rs. 10,000 is exempt from tax under Section 10(4)
(*c*) The whole of Rs. 12,000 is exempt as a casual receipt.

(*iii*) An individual in the financial year 1996-97 has donated Rs. 180 to the Prime Minister's Drought Relief Fund. No other donations were made in the year. For the assessment year 1997-98 he will be eligible for a deduction under Section 80G of the Income-tax Act, a sum of
(*a*) Rs. 180 @ 50% Rs. 90
(*b*) Rs. 100 @ 50% Rs. 50
(*c*) Rs. Nil.

(*iv*) An executive is provided with a motor car for his official as well as personal use. The standard deduction he is entitled to is :
(*a*) Rs. 3,000
(*b*) Rs. 1,000
(*c*) $33^1/_3$% of salary subject to a maximum of Rs. 15,000.

(*v*) The rate of interest accruing to a member of recognised Provident Fund on the balance in his account, in a year is 12%. In such a case
(*a*) the interest on his own contribution alone is exempt from tax
(*b*) the excess over 10% is subject to tax
(*c*) the whole interest is exempt from tax.

(*vi*) The entire amount of following payments can be claimed as deduction from business income in the same year:
(*a*) Purchase of business books for Rs. 6,000

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(*b*) Purchase of calculator for Rs. 1,000
(*c*) Purchase of equipment for Rs. 5,200.

(*vii*) Deduction u/s 80L for dividends is allowed upto (assessment year 1997-98)
(*a*) Rs. 10,000
(*b*) Rs. 15,000
(*c*) Rs. 7,000.

(*viii*) Donation for family planning is allowed as deduction at the rate of
(*a*) Nil
(*b*) 50%
(*c*) 100%.

(*ix*) An individual can claim deduction for having a medically handicapped dependent in hospital during whole of the accounting year 1996-97 for
(*a*) Rs. 4,800
(*b*) Rs. 6,000
(*c*) Rs. 15,000.

Solution

(*i*) (*b*) Taxable in India since he is an Indian citizen and he has been paid for service rendered outside India [Section 9 (*i*) (*iii*)]
(*ii*) (*a*) Rs. 12,000 is fully exempt from tax u/s 10(14)
(*iii*) (*a*) Rs. 180 @ 50% Rs. 90
(*iv*) (*c*) $33^1/_3$% of salary subject to a maximum of Rs. 15,000.
(*v*) (*c*) The whole interest is exempt from tax
(*vi*) (*a*) Purchase of business books Rs. 6,000
(*vii*) (*b*) Rs. 15,000
(*viii*) (*c*) 100%
(*ix*) (*c*) Rs. 15,000

P—8

Reproduce the correct answer:

(*i*) Salary received by a Member of Parliament is :
(*a*) exempt from tax
(*b*) taxable as salary income
(*c*) taxable as income from other sources.

(*ii*) Standard Deduction u/s 16 (*i*) on a salary income of Rs. 21,000 would be :
(*a*) Rs. 5,000
(*b*) Rs. 7,000
(*c*) Rs. 1,000.

(*iii*) Gratuity received by a Govt. employee is :
(*a*) Fully taxable
(*b*) Fully exempted
(*c*) Exempted upto Rs. 2,50,000.

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(*iv*) Perquisites and allowances paid to Govt. employees posted abroad are :
(*a*) Fully taxable
(*b*) Fully exempted
(*c*) Taxable upto 10% of employee's salary.

(*v*) Statutory limit u/s 16 (ii) for deduction of entertainment allowance in case of Govt. employee is :
(*a*) Rs. 5,000
(*b*) Rs. 7,500
(*c*) 25% of employee's salary.

(*vi*) A university teacher contributes to the :
(*a*) Statutory Provident Fund
(*b*) Recognised Provident Fund
(*c*) Unrecognised Provident Fund.

(*vii*) Computed value of pension is fully exempted in case of :
(*a*) a Govt. employee
(*b*) an employee of private sector
(*c*) an employee of a Public Sector Undertaking.

(*viii*) Value of rent free accommodation in case of Semi Govt. employee shall be taxable upto :
(*a*) 10% of employee's salary
(*b*) $12^1/_2$% of employee's salary
(*c*) $7^1/_2$% of employee's salary.

(*ix*) Reimbursement of medical bill is exempted upto :
(*a*) Full amount
(*b*) Rs. 5,000
(*c*) One month's salary of the employee.

(*x*) Dearness allowance is taxable in case of :
(*a*) All employees
(*b*) Govt. employees
(*c*) Employee of the private sector.

Solution

(*i*) Taxable as income from other sources, (*ii*) Rs. 7,000, (*iii*) Fuliy exempted, (*iv*) Fully exempted, (*v*) Rs. 5,000, (*vi*) Statutory Provident Fund, (*vii*) a Govt. employee, (*viii*) 10% of employee's salary, (*ix*) Fully exempted, (*x*) All employees.

P—9

Reproduce the correct answer:

(*i*) Agricultural income includes
(*a*) Income from interest on arrears of rent payable in respect of land used for agricultural purposes
(*b*) Income from sale of forest trees of spontaneous growth on which no operation for their preservation and growth were performed
(*c*) Income from use of land for grazing cattle required for agricultural pursuits.

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(*ii*) 'Dividends' are assessable under the head
  (*a*) Income from other sources
  (*b*) Profit & Gains
  (*c*) Capital gains.

(*iii*) Rent received from buildings held by an assessee as stock-in-trade is taxable under the head
  (*a*) Profits or gains of business or profession
  (*b*) Income from house property
  (*c*) Income from other sources.

(*iv*) A person dealing in grocery business where income exceeds Rs. 40,000 has to maintain books of account, if the turnover in any one of the three years immediately preceding the previous year :
  (*a*) Rs. 5,00,000
  (*b*) Rs. 2,00,000
  (*c*) Rs. 2,50,000.

(*v*) A Short-term Capital Asset (except shares) is the one held for not more than
  (*a*) 48 months
  (*b*) 36 months
  (*c*) 60 months.

(*vi*) Capital expenditure on scientific research which cannot be absorbed on account of insufficiency of profits in any accounting year can be carried forward for :
  (*a*) 16 years
  (*b*) 8 years
  (*c*) Indefinite period.

(*vii*) Deduction in respect of expenditure on advertisements through articles intended for presentation will be allowed on the value of each article upto a limit of
  (*a*) Rs. 1,000 + 50% of balance cost per item
  (*b*) Rs. 1,000 per item
  (*c*) Rs. 800 per item.

(*viii*) Embezzlement of cash in a money lending business shall be treated as
  (*a*) Business Expenditure
  (*b*) Revenue loss incidental to business
  (*c*) Capital Expenditure.

(*ix*) The assessee can claim the deduction from his business of any expenditure incurred by him in the previous year in respect of any appeal before any Income-tax authority upto.
  (*a*) Rs. 7,500
  (*b*) Rs. 3,500
  (*c*) Full amount.

(*x*) The entire amount of following payments will be allowed as deduction from business income in the same year:
  (*a*) Purchase of technical books for Rs. 6,000.

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(*b*) Purchase of a bicycle for Rs. 600, purchased and used in the last month of the previous year.

(*c*) Manufacture of machine for use in the factory at a cost of Rs. 8,000.

(*xi*) The salary at Rs. 6,000 per month received by Mr. Robinson Crusoe, a citizen of United Kingdom and a technician in the employment of Bharat Vyapar Ltd. will be exempt from taxation in India to the following extent and for the periods from the date of arrival in India mentioned there against :

	Exemption limit Rs.	Period from the date of arrival
(*a*)	2,400	Five years
(*b*)	4,000	Twelve months
(*c*)	4,000	Twenty-four months.

(*xii*) The deduction allowable under Section 16 (*i*) while computing the income under the head "salaries" for female employees where total income exceeds Rs. 1,00,000 for assessment year 1997-98 is a sum calculated on the basis provided hereunder.

(*a*) $33^1/_3\%$ of salary subject to a ceiling of Rs. 15,000

(*b*) $33^1/_3\%$ of salary subject to a ceiling of Rs. 18,000

(*c*) 20% of the first Rs. 10,000 of salary and 10% of the balance salary subject to ceiling of Rs. 3,500.

(*xiii*) Income from investments made outside India earned by a person not ordinarily resident in India would be taxable under the Income-tax Act, 1961 if:

(*a*) the investments are in shares of a foreign limited company.

(*b*) the investments are by way of capital contribution to a partnership business whose control and management is situated wholly outside India.

(*c*) the investment in a proprietary business carried on abroad but controlled from India.

(*xiv*) The following persons are resident in India in a previous year.

(*a*) A company—other than an Indian company—when the control and management of its affairs is situated partly in India

(*b*) A Hindu Undivided Family having business in India controlled and managed by the Karta who has been staying in Singapore

(*c*) A joint-venture between Birendra of Cuttack and Shekhar of Colombo for exporting the handicraft of Orissa. *[C.A. (Inter)]*

Solution

(*i*) (*c*) Income from use of land for grazing cattle required for agricultural pursuits.

(*ii*) (*a*) Income from other sources.

(*iii*) (*b*) Income from house property.

(*iv*) (*a*) Rs. 5,00,000.

(*v*) (*b*) 36 months.

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(*vi*) (*c*) Indefinite period.
(*vii*) (*a*) Rs. 1,000 + 50% of balance cost per item.
(*viii*) (*b*) Revenue loss incidental to business.
(*ix*) (*c*) Full amount
(*x*) (*a*) Purchase of technical books for Rs. 6,000.
(*xi*) (*c*) Rs. 4,000, Twenty-four months.
(*xii*) (*a*) $33^1/_3$% of salary subject to a ceiling of Rs. 15,000.
(*xiii*) (*c*) Investment in a proprietary business carried on abroad but controlled from India.
(*xiv*) (*c*) A joint-venture between Birendra & Shekhar.

P—10

Reproduce the correct answer:

(*i*) Income to the purchaser of standing crop (after harvesting operations are performed by him) is :
- (*a*) taxable as business income
- (*b*) exempt being agricultural income
- (*c*) included in taxable income for rate purposes only.

(*ii*) A claim of Rs. 45,000 received under the terms of consequential loss under a policy taken by a company to secure against loss of profit, is :
- (*a*) Casual receipt
- (*b*) Revenue receipt
- (*c*) Capital receipt.

(*iii*) Any compensation received by a workman under the Industrial Disputes Act or any other act is exempt upto a maximum of :
- (*a*) Total compensation received
- (*b*) Rs. 50,000
- (*c*) Rs. 20,000.

(*iv*) Jones, an Englishman staying in London, does not have any business connections in India. He, however, has earned a profit of Rs. 18,000 by sale of goods to a customer, in India by V.P.P. system. It is a profit which is received :
- (*a*) In India
- (*b*) Outside India.

(*v*) Any expenditure incurred on the purchase of Patent Rights is allowed as a deduction in equal instalments over a period of :
- (*a*) 10 years
- (*b*) 14 years
- (*c*) 8 years.

(*vi*) Blue Diamonds Ltd. incorporated in the United Kingdom :
- (*a*) Cannot be regarded as a "company" under the (Indian) Income-tax Act, 1961
- (*b*) Can be regarded as a "company" under the (Indian) Income-tax Act, 1961

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(*c*) Can be regarded as a "company" under the (Indian) Income-tax Act, 1961 if a special order is passed by the Central Board of Direct Taxes in that behalf.

(*vii*) A charity trust, to enjoy exemption, is required to get itself registered with the Commissioner of Income-tax and get its accounts audited if its income exceeds :

(*a*) the taxable minimum specified under the annual Finance Act
(*b*) Rs. 1,00,000
(*c*) Rs. 25,000.

(*viii*) A and B jointly purchased a building having specific share of 50% each. The income from this house property will be assessable :

(*a*) In the hands of the "association of persons"
(*b*) In the hands of the "association of persons" and the respective shares will be included for "rate purpose" in the hands of A and B
(*c*) In the "Individual" hands of A and B separately.

[C.A. (Inter)]

Solution

(*i*) (*a*) taxable as business income
(*ii*) (*b*) revenue receipt
(*iii*) (*c*) Rs. 50,000
(*iv*) (*a*) In India
(*v*) (*b*) 14 years
(*vi*) (*b*) can be regarded as a 'Company' under the (Indian) Income-tax Act, 1961
(*vii*) (*c*) Rs. 25,000
(*viii*) (*c*) in the individual hands of A and B separately.

P—11

(*i*) Profit on sale of licence is taxable under the head.....
(*ii*) Any capital expenditure on acquiring land for scientific research..... be debited to P & L A/c.
(*iii*) Any expenditure incurred to acquire a patent right can be written off in.....equal instalments.
(*iv*) Any expenditure incurred to acquire technical now how developed in India by an approved institution can be written off in.....years.
(*v*) Amount of expenditure incurred on preliminary expenses cannot exceed.....of capital employed.
(*vi*) In case of expenses on hotel etc. incurred by employee on tour the limit is.....
(*vii*) Maintenance of books by a professional is complusory if his *income* from such profession exceeds Rs.....in any one of the 3 years preceding the previous year.
(*viii*) It is compulsory for an assessee to get his accounts audited if his total sales turnover or gross receipts of business exceed rupees.....
(*ix*) Any payment exceeding Rs.....if made in cash is disallowed upto 20%.

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(*x*) Expenditure of maintenance of holiday homes is fully allowed if number of workers is at least.....

[**Hints :** (*i*) Profits & Gains of business or profession; (*ii*) Cannot; (*iii*) 14; (*iv*) 3 years; (*v*) $2^1/_2$%; (*vi*) Rs. 1,500 + 75% of balance; (*vii*) Rs. 40,000; (*viii*) 40 lakhs; (*ix*) Rs. 20,000; (*x*) 100]

P—12 Encircle the right choice :

I. An individual who wants to be a resident of India must stay in India for at least U/S 6(1)(a).

(*a*) 182 days

(*b*) 180 days

(*c*) 730 days in four previous years.

II. Proceeds of benefit match received by a hockey player are :

(*a*) Deductible income

(*b*) Professional income

(*c*) Casual income.

III. Perquisites and allowances paid to Government employees posted abroad are :

(*a*) Fully taxable

(*b*) Fully exempted

(*c*) Exempted if consumed abroad.

IV. Deduction in respect of expenditure on advertisements through articles for presentation will be allowed on the value of each article upto a limit of:

(*a*) Rs. 2,000 per item

(*b*) Rs. 1,000 per item

(*c*) Rs. 1,000 + 50% of amount exceeding Rs. 1,000 per item.

V. Wealth Tax Act is applicable to

(*a*) Whole of India

(*b*) Whole of India except State of J & K.

(*c*) Whole of India except the State of Sikkim.

VI. Under Central Sales Tax Act, the burden of proof in case the movement does not amount to sale is on the :

(*a*) Customer

(*b*) Dealer

(*c*) Assessing authority.

***Answer whether following statements are true or false*:**

VII. Capital receipts cannot be treated as taxable incomes.

VIII. An H.U.F. is resident in India only if the control and management of its affairs is situated wholly in India.

IX. The interest credited to Public Provident Fund is fully exempted.

X. Commission paid to bank for collection of dividend warrants is deductible for computing profits and gains of business and profession.

XI. Perquisites cannot be given in monetary form.

XII. Units of mutual funds are eligible for exemption from wealth-tax only if these are kept for six months as on valuation date.

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XIII. Gifts are voluntary transfer of property without consideration.

XIV. Declared goods are exempted from sales tax.

Fill in the blanks with appropriate words:

XV. Embezzlement of cash in a money lending business would..... for computing business profits.

XVI. Income received as rent from subletting would be taxable under the head.....

XVII. Expenditure incurred by an Indian company on acquisition of patents and trade marks can be amortised equally in.....years.

XVIII. The computation of firm's income is done first as income is computed under the head.....U/S 28.

XIX. Goods of special importance in inter-state trade or commerce are called.....

XX. Gift tax is a.....tax.

Give one word answer to the following questions:

XXI. Who is a person liable to pay any tax or any other sum of money under the Income-tax Act.

XXII. Under which head profit arising from the transfer of shares held as stock in trade taxable ?

XXIII. How would you treat an expenditure shown by the assessee in his books for which he does not give satisfactory explanations ?

XXIV. How would you call sale of goods sent by V.P.P. from Delhi to Chandigarh ?

XXV. How would you call the excess of assets owned by the assessee over the debts owed by him on the valuation date ?

[**Hints :** I (*a*), II (*c*), III (*b*), IV (*c*), V (*a*), VI (*b*), VII (True), VIII (False), IX (True), X (False), XI (False), XII (False), XIII (True), XIV (False), XV (be allowed), XVI (other sources, XVII (14 years), XVIII (Profits & Gains of Business or Profession), XIX (declared goods), XX (Direct/Personal), XXI (Assessee), XXII (Profits & Gains of Business or Profession, XXIII (Deemed Income), XXIV (Inter-state sale), XXV (Net wealth)

[P.U. B.Com. April 1993]

P—13 Encircle the right choice

I. Average rate of income-tax means—

(*a*) The rate arrived at by dividing the amount of income-tax calculated on the total income by such total income

(*b*) The rate arrived at by dividing the total of different rates of tax by the number of such tax rates.

(*c*) None of the above.

II. The term previous year means :

(*a*) The accounting period of the assessee

(*b*) Financial year before the assessment year

(*c*) Calendar year before the assessment year

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III. Medical allowance received by an employee is

(*a*) Fully taxable

(*b*) Fully exempt

(*c*) Exempted upto the amount of actual expenditure incurred on medical treatment.

IV. The term cash credits under income tax is :

(*a*) Refund of tax

(*b*) Deemed income

(*c*) Short term bank credit.

V. Wealth tax is

(*a*) Personal and direct tax

(*b*) Indirect tax

(*c*) None of the above.

VI. Under Central Sales-tax Act certificate for registration is granted in

(*a*) Form B

(*b*) Form C

(*c*) Form D.

Answer whether following statements are true or false :

VII. Premium on issue of new shares in a capital receipt.

VIII. A person can be a resident of more than one country.

IX. Death cum retirement gratuity received by a Central Government employee is fully exempted.

X. In respect of government employees entertainment allowance is partially exempted.

XI. Rent paid by a partnership firm to one of its partners for using his house for the business of the firm is not an admissible deduction.

XII. Assessment made under section 144 of Income tax Act is known as discretionary best judgement assessment.

XIII. Income tax authorities shall act as authorities under Wealth-tax act.

XIV. Goods carried by the assessee personally in pursuance to agreement to sell to other state is inter-state sale.

Fill in the blanks with appropriate words:

XV. A person liable for tax on income of other person is known as.....

XVI. Casual incomes are exempted upto a total of Rs. .....in a previous year.

XVII. An asset used in business for a period less than 180 days in the previous year would be entitled to.....of the prescribed rate of depreciation.

XVIII. The personal expenses of the assessee are.....deductions for computing business profits.

XIX. Valuation date is.....immediately before the assessment year.

XX. Central Sales Tax Act came into force on.....

Give one word answer to the following questions:

XXI. Who is an assessee failing to fulfil his statutory obligations ?

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XXII. Under which section profits arising from an isolated transaction treated as adventure in the nature of trade, taxable ?

XXIII. Can stock in trade held by the assessee for five years be treated as a capital asset.

XXIV. What is the rate of deduction of tax at source on interest paid on debentures issued by a private sector company.

XXV. How are the gifts made in contemplation of death known as ?

[B.Com. P.U. Sept. 1993]

[**Hints** : I (*a*), II (*b*), III (*a*), IV (*b*), V (*a*), VI (*a*), VII (T), VIII (T), IX (T), X (F), XI (F), XII (F), XIII (T) XIV (T) XV Representative assessee, XVI Rs. 5,000 XVII $^1/_2$, XVIII Inadmissible, XIX 31st March, XX 5th Jan. 1957, XXI Assessee-in-default XXII Section 28, XXIII No, XXIV 10% or 20% XXV Mortis Causa.

P—14 Encircle the right choice

I. Fair market value in relation to capital asset means the price :

(*a*) That is realised on its sale in the market.

(*b*) That the capital asset would ordinarily fetch on sale in the open market on the relevant date.

(*c*) Arrived at by way of bargaining between a knowledgeable buyer and a knowledgeable seller.

II. Subsidy received from Government under scheme for promotion of industry is a

(*a*) Revenue receipt (*b*) Capital receipt

(*c*) None of the above.

III. Income accruing in India but received outside India is taxable in respect of

(*a*) Only resident assessees (*b*) Only non-resident assessees

(*c*) All types of assesses.

IV. In the case of employees covered by payment of Gratuity Act 1972, the maximum exemption for retirement gratuity is :

(*a*) Rs. 50,000 (*b*) Rs. 1,00,000

(*c*) Rs. 75,000.

V. Ground rent as per section 24(I) (v) for computing income from house property is deduction on

(*a*) Payment basis (*b*) Receipt basis

(*c*) Accrual basis.

VI. Gift tax is applicable to

(*a*) Whole of India (*b*) Whole of India except State of J & K

(*c*) Whole of India except the State of Sikkim.

VII. Under Central Sales Tax Act the list of declared goods is provided under section

(*a*) 14 (*b*) 15

(*c*) 13.

VIII. Guest house buildings under Wealth Tax Act are :

(*a*) Taxable (*b*) Non-Taxable

(*c*) Taxable if used as a hotel.

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Answer whether following statements are true or false:

IX. Gift of movable property in J & K is taxable if it is made by a person who is non-citizen and non-resident of India.

X. Investment allowance is not admissible in respect of plant or machinery installed after March 31, 1990.

XI. Interest on debentures of a company is deductible U/S 80L subject to a maximum of Rs. 10,000.

XII. Net wealth of a mutual fund is taxable under Wealth Tax Act.

XIII. Inter-state sales means movement of goods from one state to another.

XIV. Commission received by landlord for selling produce for and on behalf of the tenant is an agricultural income.

XV. Any payment exceeding Rs. 10,000 made otherwise than by crossed account payee cheque or draft shall be disallowed for computing business profits.

XVI. From the assessment year 1993-94 a partnership firm cannot be assessed as association of persons.

XVII. The term capital asset (Section 2(14)) includes only tangible property.

Fill in the blanks with appropriate words:

XVIII. All those assets to which one rate of depreciation is applicable are known as.....

XIX. Any income not included for computing gross total income is known as.....

XX. Any person receiving a gift is known as.....

XXI. The preliminary expenses of an Indian company can be amortised equally in.....years.

XXII. Deduction in respect of repairs is restricted to.....of net annual value.

XXIII. Valuation date is.....immediately preceding the assessment year.

XXIV. The due date of filing return of income by a salaried assessee is.....

XXV. Exemption regarding capital gains from the transfer of land used for agricultural purposes (Sec 54 B) is admissible to.....assessees only.

[*B.Com. P.U. Sept. 1994*]

[**Hints :** I (*b*), II (*b*), III (*c*), IV (*b*), V (*c*), VI (*b*), VII (*a*), VIII (*a*), IX (F), X (T), XI (F), XII (F), XIII (T), XIV (F), XV (T), XVI (F), XVII (F), XVIII Block of assets, XIX Exempted Income, XX Donee, XXI 10 years, XXII $^1/_5$th, XXIII 31st March, XXIV 30th June, XXV Individual and H.U.F]

P—15 Encircle the right choice

I. Bonus shares received by a dealer of shares is a :

(*a*) Capital receipt
(*b*) Revenue receipt
(*c*) Exempt income.

II. Transferred Balance is

(*a*) The balance in the unrecognised provident fund at the time of its conversion into recognised provident fund.
(*b*) Balance transferred from one bank account to other
(*c*) Compensation at the time of transfer of an employee

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III. The maximum amount of exemption of compensation received at the time of voluntary retirement U/S 10 (10 C) is

(*a*) Rs. 1,00,000
(*b*) Rs. 80,000
(*c*) Rs. 5,00,000.

IV. Interest payable outside India on a loan for the construction of House property is deductible for computing Income from house property if

(*a*) Property is let out
(*b*) Property is self occupied
(*c*) If tax on interest is deducted at source.

V. Capital gains arising from the transfer of agricultural land owned for five years in a rural area are :

(*a*) Taxable as short term capital gain
(*b*) Taxable as long term capital gain
(*c*) Exempt.

VI. Tax rebate for senior citizen (sec. 88 B) is available from assessee who has attained the age of :

(*a*) 60 years
(*b*) 65 years
(*c*) 58 years.

VII. Right to enforce partition of an H.U.F. is available to

(*a*) Only male members
(*b*) Only female members
(*c*) Both male as well as female members.

VIII. A residential plot in urban area acquired a year back on which no construction has taken place is

(*a*) Taxable under wealth tax act
(*b*) Not taxable
(*c*) Not taxable if owned by a resident assessee.

Answer whether following statements are true or false:

IX. Value of self occupied house is taken as the fair market value on the valuation date.

X. Gift inter vivos are taxable.

XI. The term 'Sale' includes transfer under hire purchase agreement.

XII. Sale of goods sent by V.P.P. from Chandigarh to Mohali is inter-state sale.

XIII. If an assessee fails to pay advance tax, he can be fined up to Rs. 1,000.

XIV. From the assessment year 1993-94 a partnership firm can not be assessed as association of persons.

XV. Loss incurred in speculative business in banned items cannot be carried forward to the next year.

XVI. Income by way of interest on securities held as stock in trade is taxable under the head income from other sources.

XVII. Exemption for capital gains arising from the transfer of land used for agricultural purposes (Sec. 54 B) is available to individuals and HUF assessees.

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Fill in the blanks with appropriate words:

XVIII. All those assets to which one rate of depreciation is applicable are known as.....

XIX. Income from the business of owning and letting out house properties is taxable under the head.

XX. U/s 27(iv) a charge to secure an annual liability is known as.....

XXI. Any compensation received by an employee from his employer at the time of termination of employment is known as.....

XXII. An income not included in gross total income is known as.....

XXIII. Person leaving India must be assessed in the.....

XXIV. Any person making a gift is known as.....

XXV. The sales tax levied on exports from India is.....

(B.Com. P.U. April, 1995)

[**Hints :** I (*b*), II (*a*), III (*c*), IV (*c*), V (*c*), VI (*b*), VII (*c*), VIII (*a*), IX (F), X (T), XI (T), XII (T), XIII (F), XIV (F), XV (T), XVI (T), XVII (F), XVIII Block of assets, XIX House Property, XX Annual charge, XXI Profit in lieu of salary, XXII Exempted, XXIII same previous year, XXIV Doner, XXV Central Sales Tax/or Export Duty.]

P—16 Encircle the right choice as given in the example below :

Example : Two and Two make: (In this example c is correct) (*a*) 6 (*b*) 5 (*c*) 4

I. Salary paid by the Government to a citizen of India for service rendered outside India is:

(*a*) Income accruing in India

(*b*) Income deemed to accrue in India

(*c*) Income accruing outside India.

II. Income of a newly set up business from 1st October to 31st March, 1997 is assessable in the assessment year:

(*a*) 1995-96

(*b*) 1996-97

(*c*) 1997-98.

III. An assessee is holding shares as his stock in trade. Dividend received by him is taxable under the head :

(*a*) Profits and gains of business

(*b*) Income from other sources

(*c*) None of the above.

IV. Unabsorbed depreciation can be carried forward for set off :

(*a*) For a period of 4 years

(*b*) For a period of 8 years

(*c*) For an unlimited time.

V. While computing the income under the head 'salaries' standard deduction of Rs. 18,000 is allowed to a woman assessee whose total income doesn't exceed :

(*a*) Rs. 60,000

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(*b*) Rs. 75,000

(*c*) Rs. 1,00,000.

VI. In Case of Hindu undivided family which has at least one member whose individual total income exceeds Rs. 40,000 nil slab for assessment year 1997-98 is :

(*a*) Rs. 15,000

(*b*) Rs. 40,000

(*c*) Rs. 18,000.

VII. Under Central Sales Tax Act, Registration certificate is granted in:

(*a*) Form B

(*b*) Form C

(*c*) Form D.

VIII. Under the Gift Tax Act. taxable gift is :

(*a*) Gift Inter Vivos

(*b*) Gift Mortis Causa

(*c*) Gift under a Will.

IX. Wealth tax is applicable to :

(*a*) Whole of India except the state of Jammu and Kashmir

(*b*) Whole of India except the state of Sikkim

(*c*) Whole of India.

QUESTIONS X-XVIII

Answer whether the following statements are true or false:

X. Salary paid to a partner of a firm is chargeable to tax under the head 'Profits and gains of business and profession'.

XI. Deduction under section 80G is granted only when aggregate donations exceed Rs. 500.

XII. Dividend recieved by share holder out of the agricultural income of a company, is agricultural income.

XIII. Remuneration recieved by a teacher of a university for evaluating answer books of the same university is chargeable to tax under the head 'salaries'.

XIV. A firm is resident in India except where the control and management of its affairs is situated wholly outside India.

XV. Declared goods are exempt from Sales Tax, under the Central Sales Tax Act.

XVI. Credit for stamp duty paid is given under section 18A of Gift Tax Act, before the rebate on advance tax paid is allowed under section 18.

XVII. Jewellery, which is stock in trade, is included in 'assets' under the Wealth Tax Act.

XVIII. For the assessment year 1997-98, cost of acquisition of Bonus Shares, for the computation of capital gain will be taken as 'NIL'.

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QUESTIONS XIX-XXV

Fill in the blanks with appropriate word/words.

XIX. Loss under the head 'capital gains' can be carried forward for ..... years.

XX. Any payment exceeding Rs.....if made in cash is disallowed upto 20%.

XXI. Any expenditure incurred for acquiring 'known how' developed in India by an approved institution can be written off in.....years.

XXII. In case of individuals tax on long term capital gains charged at the rate of.....

XXIII. Assets belonging to the assessee on the.....are taxable under the Wealth Tax Act.

XXIV. 'Donee' means any person who.....any property under a gift.

XXV. Goods of special importance in inter state trade or commerce are called..... *[B.Com. Punjab Oct. 1995]*

[**Hints** : I (*b*), II (*c*), III (*b*), IV (*b*), V (*b*), VI (*b*), VII (*a*), VIII (*a*), IX (*c*), X (T), XI (F), XII (F), XIII (T), XIV (T), XV (F), XVI (T), XVII (F), XVIII (T), XIX (8 years), XX (Rs. 10,000), XXI (3 years), XXII (20%), XXIII (Valuation date), XXIV (Acquires), XXV (Declared goods).

P—17 QUESTIONS I-VIII

Encircle the right choice as given in the example below :

Example : Two and two make :

(in this example *c* is the right choice)

(*a*) 6
(*b*) 5
(*c*) (4)

I. Reduction admissible from tax liability is known as

(*a*) Exemption
(*b*) Deduction
(*c*) Rebate.

II. Salary paid by the Govt. to a citizen of India for services rendered outside India is :

(*a*) Income accruing in India
(*b*) Income deemed to accrue in India
(*c*) Income accruing outside India.

III. An assessee is holding debentures of a Joint Stock Company as stock in trade. Interest received by him is taxable under the head,

(*a*) Profit and gains of business
(*b*) Income from other sources
(*c*) None of the above.

IV. Deduction u/s 80GG is admissible in respect of

(*a*) House rent received from the employer

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(*b*) House rent paid

(*c*) House tax paid.

V. Unabsorbed speculation business loss can be carried forward for set off :

(*a*) For a period of 4 years

(*b*) For a period of 8 years

(*c*) For an unlimited period.

VI. The due date of first instalment of advance tax by assessees other than companies is :

(*a*) 15th June

(*b*) 15th September

(*c*) 30th June.

VII. Under Central Sales Tax Act, registration certificate is granted in:

(*a*) Form A

(*b*) Form B

(*c*) Form C.

VIII. Under the Gift Tax Act, taxable gift is :

(*a*) Gift Inter Vivos

(*b*) Gift Mortis Causa

(*c*) Gift under a will.

QUESTIONS IX-XVIII

Answer whether following statements are true or false:

IX. When dividend is paid to a domestic company shareholder, tax is deducted at source @ 21.5%.

X. Under Section 72 (A) losses of amalgamating company can be carried forward by amalgamated company.

XI. A firm is resident in India except where the control and management of its affairs is wholly situated outside India.

XII. Income derived from sale of grass of spontaneous growth is agricultural income.

XIII. Compensation received due to the termination of employment is taxable under Income from other sources.

XIV. In the case of income in the nature of family pension a deduction of a sum equal to 33-$^1/_3$% of such income or Rs. 12,000 whichever is less is admissible.

XV. Deduction u/s 80G is granted only when aggregate of donations exceed Rs. 500.

XVI. Declared goods are exempt from Sales Tax.

XVII. Gain arising from the sale of Motor Car meant for personal use in not taxable.

XVIII. Credit for stamp duty paid is given under Section 18A of Gift Tax Act before rebate on advance tax paid is allowed under Section 18

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QUESTIONS XIX-XXV

Fill in the blanks

XIX. Loss under the head capital gains can be carried forward for .....years.

XX. Deduction u/s 35D is spread over.....years in equal instalments.

XXI. Assets belonging to the assessee on the..... are taxable under the Wealth Tax Act.

XXII. The assessee making a taxable gift is known as.....

XXIII. Any payment exceeding Rs.....is made in cash is disallowed upto 20%.

XXIV. An employee of a company who is a director thereof is considered as.....

XXV. Income from subletting a house is taxable under the head.....

[Panjab B.Com. April. 1996]

[**Hints :** I (*c*), II (*b*), III (*b*), IV (*b*), V (*b*), VI (*b*), VII (*b*), VIII (*a*), IX (T), X (T), XI (T), XII (F), XIII (F), XIV (T), XV (F), XVI (F), XVII (T), XVIII (T), XIX (8 years), XX (10 years), XXI Valuation Date, XXII Donor, XXIII Rs. 20,000, XXIV Specified person, XXV Income from Other sources]

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4 SHORT QUESTIONS

These questions can carry upto 5% marks in a question paper.

Agricultural Income

Q. 1. Compute the tax liability of Mr. X for the assessment year 1997-98 if—

(*a*) his agricultural income is Rs. 50,000; and

(*b*) his non-agricultural income is Rs. 46,000.

[**Hints :** Rs. 1,800]

Q. 2. Compute the tax liability of an H.U.F. for the assessment year 1997-98 if—

(*a*) its agricultural income is Rs. 39,540; and

(*b*) its non-agricultural income is Rs. 46,560.

Karta's son is working in an office and his taxable income for the year is Rs. 46,050.

[**Hints :** Rs. 1,968]

Q. 3. Compute the tax liability of Mr. K.N. Singh of Darbhanga for the assessment year 1997-98 if—

(*a*) his agricultural income is Rs. 39,450 and

(*b*) his non-agricultural income is Rs. 1,09,050.

[**Hints :** Rs. 23,565]

Residential Status

Q. 4. Determine the residential status of Mr. X for the previous year 1996-97 who left India for the first time on 15.9.92 and came back on 1.9.95. He again left for Dubai on 15.6.96 to come back on Feb. 14, 1997 to settle in India for ever.

[**Hints :** Resident u/s 6 (1) (*b*) but not ordinarily resident u/s 6(6)]

Q. 5. Mr. Heynes, a West Indian, came to India for the first time on 10.1.1993 and left for Australia on 15.9.1993. He again came to India on 1.5.1996 to leave for South Africa on 15.6.1996. Determine his status for the previous year 1996-97.

[**Hints :** Non-Resident]

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Q. 6. Mr. Singh, shifted from India on 15th Nov. 1995 to U.K. to settle there. He came back to India on 15th Dec. 1996 to attend to last rites on the death of a relative and was to go back on 1st Jan. 1997 but due to illness stayed in India till 28th Feb. 1997. The Assessing Officer wants to treat him as Resident for the previous year 1996-97. Is he correct ?

[**Hints :** Yes, Mr. Singh is Resident u/s 6(1)(b)]

Q. 7. An H.U.F. managed by Mr. Kamal has income in India as well as from outside India. Mr. Kamal and his family are staying in Dubai for the last 4 years. The family has property in India. What will be the residential status of H.U.F. for the previous year 1996-97 if—

(*a*) the affairs of H.U.F. are wholly managed from Dubai; or

(*b*) the affairs of H.U.F. are partially managed in India.

[**Hints :** (*a*) HUF is Non-resident, (*b*) HUF is Resident but N.O.R.]

Q. 8. Mr. Y after 30 years stay in India retires to America on February 3, 1994. He returns to India in July 1996 to join an American company as its overseas branch manager. Determine his residential status for the assessment year 1997-98. *[Kalyani University B.Com. 1991]*

[**Hints :** Resident u/s 6(1)(*a*) but N.O.R. u/s 6(6)]

Q. 9. H, got a job at Kuwalalampur. He left for Kuwalalampur on 30th September 1994. He never left India earlier. What was his residential status for the previous year 1996-97] *[Kalyani University, B.Com. 1990]*

[**Hints :** Non-resident]

Q. 10. Mr. A came to India for the first time from U.S.A. on 30th June 1990. He stayed here at a stretch for three years and left for Japan on 1st July 1993. He returned to India on first April 1994 and remained here till 31st July 1994 when he went back to U.S.A. He again came to India taking an employment with an American concern on 20th January 1997. Determine his residential status for the assessment year 1997-98.

[Punjab University B.Com. 1992]

[**Hints :** Resident but NOR u/s 6(6)]

Exempted Incomes

Q. 11. Calculate the amount of exemption available u/s 10(3) in following cases separately—

(*i*) Lottery prize of Rs. 1,00,000

(*ii*) Crossword puzzle prize of Rs. 3,600

(*iii*) Race winnings in June 1996 Rs. 12,000

(*iv*) Race winnings in January 1997 Rs. 30,000.

[**Hints :** (*i*) Rs. 5,000; (*ii*) Rs. 3,600; (*iii*) Rs. 2,500; (*iv*) 2,500]

Q. 12. Calculate the amount of exemption of leave travel concession u/s 10(5) in each of the following cases separately :

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(*i*) Rs. 5,650 allowed to Mr. Z a Govt. of India employee for going to Nainital in the block period of 1.1.1996 to 31.12.1997.

(*ii*) Rs. 10,450 allowed to Mr. X for going to Goa in June 1991 (Block period 1.1.1986 to 31.12.1989) and Rs. 14,600 in Nov. 1996 for going to Darjeeling for the block period commencing on 1.1.94.

(*iii*) Mr. Sood receives one month salary each year as Leave Travel allowance without spending any thing. During December 1996 he received Rs. 3,900 as Leave Travel allowance.

(*iv*) Mr. Shankar received Rs. 2,500 as Leave Travel allowance but he actually spent Rs. 2,000 in the year on going to his home town.

[**Hints :** (*i*) Rs. 5,650; (*ii*) Rs. 14,600; (*iii*) No exemption; (*iv*) Rs. 2,000]

Salaries

Q. 13. Calculate the amount of basic salary of a Lecturer for the previous year 1996-97 who is appointed on 1.1.1991 in the grade of Rs. 2,200-100-3,000-125-4,000. He gets increment after every 12 months and salary is due on 1st of every month.

[**Hints :** Rs. 32,600]

Q. 14. Calculate the amount of basic salary for the previous year 1996-97 of an officer of a public sector undertaking who is appointed on 1.9.1992 in the grade of Rs. 5,000-200-5,600-300-6,500. He gets his increment after every twelve months and his salary is due on the last date of the month.

[**Hints :** Rs. 69,300]

Q. 15. Prof. Basu does not want to withdraw his salary due on 1.3.1997. He claims that 11 month's salary should be considered for tax purposes. Advise Prof. Basu. *[Kalyani University B.Com. 1991]*

[**Hints :** 12 months salary is taxable whether received or due]

Q. 16. Calculate the amount of taxable annual accretion to RPF for Mr. X, from the particulars given below :

(*i*) Salary @ Rs. 3,500 p.m.

(*ii*) D.A. @ Rs. 1,000 p.m. (Rs. 500 p.m. enters into pay for service benefits)

(*iii*) He and his employer contribute Rs. 500 p.m. (each) to RPF

(*iv*) Interest credited to accumulated balance of RPF @ 14% is Rs. 8,400.

[**Hints :** Rs. 1,200 + Rs. 1,200 = Rs. 2,400]

Q. 17. Calculate the taxable portion of URPF to RPF from particulars given below :

(*i*) Contribution to URPF from 1.4.1994 to 30.6.1996 @ Rs. 400 p.m. (each) by employer and employee

(*ii*) Interest credited @ 14% for the period is Rs. 4,200.

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(*iii*) His salary during this period was Rs. 3,000 p.m. (consolidated) due on last date of month.

[**Hints :** Rs. 3,300 under the head 'Salaries']

Q. 18. An individual received House Rent Allowance @ Rs. 300 p.m. from his employer. He paid house rent @ Rs. 500 p.m. for his hired accommodation at Bhubneshwar. His basic pay was Rs. 1,600 p.m. and dearness allowance was Rs. 1,000 p.m. Find out his taxable house rent allowance for the assessment year 1997-98. *[Kalyani University B.Com. 1990]*

[**Hints :** Full amount of Rs. 3,600 is exempted]

Q. 19. Mr. Tarakaram, posted at Ernakulam receives from employer emoluments consisting of basic pay Rs. 36,000, bonus Rs. 3,600, project allowance Rs. 2,400 and overtime allowance Rs. 1,000 during the year 1996-97. His employer has provided him with a furnished accommodation at concessional rent of Rs. 200 p.m. Furniture was hired at an annual charge of Rs. 4,000 and some items of furniture were purchased for Rs. 40,000 for the accommodation by the employer. The fair rent of the house is Rs. 20,000 p.a. Calculate the value of perquisite.

[Kalyani University B.Com. 1991]

[**Hints :** Rs. 9,900]

Q. 20. Mr. X is working as an officer with Central Govt. at Delhi. His salary for the year 1996-97 is Rs. 48,000. He is getting D.A. at the rate of 70% of salary and D.A. upto 40% of salary is treated as pay for service benefits. He is provided with rent free house whose rental value is Rs. 350 p.m. Calculate the value of rent free house.

[**Hints :** Rs. 4,200]

Q. 21. Mr. Alma's monetary emoluments from Shanbhog Ltd. amount to Rs. 18,000 p.a. He is provided with a free car for his private use. The expenses on running and maintenance spent by the company being Rs. 5,000. Compute the value of perquisite of car.

[Punjab University B.Com. 1992]

[**Hints :** Car is exempted as employee is not covered u/s 17(2)(*iii*)]

Q. 22. Ping served HH Ltd. during the previous year 1996-97. His employer provided him with a 20 HP motor car for private as well as official use. The employer paid driver's wages. The employer also paid the running and maintenance expenses. Determine the taxable perquisite of Ping, if any :

(*i*) Suppose that Ping's basic salary and dearness allowance during the previous year 1996-97 were Rs. 50,000, or

(*ii*) Suppose that Ping's total salary excluding all non-monetary benefits was Rs. 22,000 during the previous year 1996-97.

[Kalyani University B.Com. 1990]

[**Hints :** (*i*) Taxable value Rs. 9,600 + Rs. 3,600 = Rs. 13,200; (*ii*) Taxable value is Nil as he is not covered u/s 17(2)(*iii*)]

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Q. 23. Mr. M gives the following particulars of his income earned during the year ended 31st March, 1997 :

		Rs.
(*i*)	Net Salary received	16,000
(*ii*)	Tax deducted at source by the employer	2,000
(*iii*)	Own Contribution to R.P.F. (Equal amount contributed by the employer)	2,400
(*iv*)	'M' was provided with a 20 H.P. Car both for employment as well as private purpose.	

Compute income from Salary of Mr. M for the assessment year 1997-98.
[Kalyani University B.Com. 1991]

[**Hints :** Salary Income Rs. 13,840; Car exempted.]

Q. 24. Rao, a Bank Manager, gets Rs. 2,000 per month as salary and dearness allowance at 10 per cent of the salary. He is getting entertainment allowance of Rs. 6,000 p.a. since 1953. During the previous year ended 31st March, 1997 he received a bonus of three months' salary. Besides he is also provided with a rent-free house whose fair rent is Rs. 500 per month. Find out his income under the head 'Salaries' for the Assessment Year 1997-98. *[Nagarjuna B.Com March, 1995]*

[**Hints :** Salary Income Rs. 22,880]

Q. 25. The following are the particulars of the income of Sirisha, a Government Servant for the year ended 31st March. 1997 :

(*a*) Basic pay Rs. 3,000 p.m.
Dearness Allowance Rs. 2,000 p.m.
House Rent Allowance Rs. 900 p.m. (Actual rent paid Rs. 800 p.m.).

(*b*) She and her employer contribute Rs. 450 p.m. to R.P.F.

(*c*) Interest credited to her R.P.F. balance @ 14% amounted to Rs. 9,800.

(*d*) During the year she paid Rs. 400 as professional tax. Compute her salary income.

[**Hints :** Salary Income Rs. 49,600]

Q. 26. From the following salary particulars of Mr. Raju, calculate his salary income for the assessment year 1997-98.

Basic pay Rs. 3,000 per month.

Dearness Allowance Rs. 2,000 per month.

House Rent Allowance Rs. 500 per month (actual rent paid Rs. 400 per month).

Own contribution to R.P.F. — 10% of salary.

Employer's contribution to R.P.F. — 15% of salary.

He paid Rs. 200 towards professional tax during the previous year.

[**Hints :** Salary Income Rs. 51,400]

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Q. 27. (*a*) From the following particulars, compute Taxable House Rent Allowance and salary income. Salary Rs. 5,000 p.m., H.R.A. Rs. 1,500 p.m., Actual Rent paid in Bombay : Rs. 3,000 p.m.

(*b*) Mr. X gets a salary of Rs. 5,000 p.m. and is provided with rent-free unfurnished house whose rental value is Rs. 2,000 p.m. Calculate the value of Rent-free house and salary income.

[**Hints :** (a) Taxable HRA Nil, salary income Rs. 42,000 (b) Value of rent-free house Rs. 6,000, salary income Rs. 51,000]

Q. 28. (*a*) Mr. Sri Hari is working with a private firm drawing a monthly salary of Rs. 5,000 and Entertainment Allowance of Rs. 500 p.m. since 1.4.1952. Compute taxable portion of Entertainment Allowance and salary income.

(*b*) Mr. Z is working with Vazir Sultan Company and is provided with a big motor car which is used for personal and official use and all the expenses are met by the Company. Find out the value of the car.

[Osmania B.Com. Nav. 1995]

[**Hints :** (a) Taxable E.A. NIL; Salary income Rs. 45,000; (b)Value of car Rs. 9,600]

Q. 29. Sri. Achuta, an employee of ABC (P) Ltd. receives Rs. 1,05,400 as leave salary at the time of his retirement on January 31, 1997. Determine the amount of taxable leave salary from the following Information :

Salary at the time of retirement	Rs. 3,100
Average salary received during 10 months ending on January 31.1.1997	Rs. 3,000
Duration of service	$24^3/_4$ yrs.
Leave entitlement for every year of service	$1^1/_2$ months
Leave availed while in service	2 months
Leave at the credit of the employee at the time of retirement ($24 \times 1^1/_2 - 2$)	34 months
Leave Salary paid at retirement at the rate of Rs. 3,100 per month (Rs. 3,100 × 34)	Rs. 1,05,400

[Bangalore B.Com. April, 1995]

[**Hints :** Taxable leave salary Rs. 81,400]

Q. 30. Mr. Prakash retires in September 1996 after having put in 42 years of service in a company. His average salary for 10 months preceding September 1997 is Rs. 2,500 P.M. He receives a gratuity of Rs. 60,000. Compute his taxable gratuity. *[Bangalore B.Com. April, 1992]*

[**Hints :** Taxable gratuity Rs. 7,500]

Q. 31. Ajay, an employee of a company at Chandigarh is in receipt of a monthly salary of Rs. 3,000. In addition he is also entitled to bonus equivalent to two months salary and an amount of Rs. 300 p.m. (W.E.F. 1.4.1964) as an

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entertainment allowance. He is provided with a rent free accommodation (unfurnished). Annual rental value of this type of accommodation in the same locality is Rs. 5,000, while the rental value according to the municipal records is Rs. 6,000. His gardener's salary of Rs. 100 p.m. is also borne by the employer. Educational expenses of his son in the U.K. amounting to Rs. 5,000 have been met by the employer.

Find out his total income from salary. *[Panjab B.Com. April, 1996]*

[**Hints :** Gross salary Rs. 55,160 ; Standard Deduction Rs. 18,000 ; Salary Income Rs. 37,160]

House Property

Q. 32. Mr Satish an employee of a private publicity agency gets Rs. 48,000 as basic pay p.a. Rs. 3,000 as commission on his turnover Rs. 4,000 as bonus, Rs. 8,000 as project allowance and Rs. 6,000 as conveyance allowance (one-third of which is utilised for official purposes). His employer also pays Professional Tax of Rs. 3,000 on behalf of Satish, Besides this the employer provides a rent-free unfurnished house in Agra, Fair rent of the house is Rs. 35,950. Determine the taxable value of the perquisite for the Asst. year 1997-98. *[Bangalore B.Com. Nov. 1993]*

[**Hints :** Value of rent free house Rs. 7,950]

Q. 33. Gopal is the owner of a house property whose Municipal valuation is Rs. 25,000. The construction of the property was commenced on 1st January, 1989 and completed on 30th April. 1991. The building comprise of three residential Units and is let out to X, Y, and Z on a annual rent of Rs. 10,000 per unit. Gopal pays Municipal Taxes Rs. 3,000 for the entire building. Find out the adjusted annual value of each unit if X and Y have taken their Units for residential purposes and Z for the business purpose.

[Nagarjuna B.Com. March, 1995]

[**Hints :** Net Annual Value Rs. 26,400]

Q. 34. Mr. Kasi owns a house property. Its annual letting value is Rs. 9,000. During the previous year it was let out to a tenant on a monthly rent of Rs. 800. Other particulars of this house property are as below :

	Rs.
Municipal taxes paid	1,000
Ground Rent	200
Fire Insurance	300
Repairs	300
Collection charges	100

Compute income from house property for the A.Y. 1997-98 assuming that the construction of the house property was completed on 1st May 1993. *[Nagarjuna B.Com. Sept. 1995]*

[**Hints :** Income from house Property Rs. 6,380]

Q. 35. From the particulars given below, compute taxable income from house property for the previous year 1996-97: Annual rental value– Rs. 6,000, Municipal value–Rs. 5,000, Municipal taxes paid by the owner–Rs. 1,200, Ground rent – Rs. 60, Fire insurance pre-mium on property–Rs. 50,

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Collection charges – Rs. 500, Unrea-lised rent allowed earlier received during the year – Rs. 2,500. The house remained vacant for 2 months during the year. *[Bangalore B.Com. April, 1992]*

[**Hints :** Income from house property Rs. 2,930 + Unrealised rent recovered Rs. 2,500 = 5,430]

Q. 36. From the particulars given below compute the total income of Mr. Rahi for the assessment year 1997-98 :

(*i*) Rent from house	24,000 p.a.
(*ii*) Municipal Rental value	18,000 p.a.
(*iii*) Local Taxes	1,800 p.a.
(*iv*) Fire Insurance Premium	600 p.a.
(*v*) Interest on Loan	2,000 p.a.
(*vi*) B/F loss from house property	
A.Y. 1993-94	10,000
A.Y. 1994-95	20,000
(*vii*) His other Income	49,500

[**Hints :** H.P. income Rs. 15,160]

Q. 37. A company manufacturing steel constructed a new building on 31.3.1992 at a cost of Rs. 4,00,000, there being eight units equal in all respects. In four of these, the company's offices were situated, one was let out to its factory manager at a subsidised rent of Rs. 400 per month, the reasonable rent being Rs. 600 per month. Two were let out to a stationery shop at a rent of Rs. 600 per month for each unit and the eigth units was let out to an individual for the purpose of his residence at a rent of Rs. 600 p.m. If the expenses for the entire building were as under, then assuming that these are to be evenly allocated to the units, determine giving reasons, wherever necessary, the income from house property.

	Rs.
Interest on loan for constructing the house	8,000
Expenses on repairs	2,400
Fire Insurance Premium	1,600
Municipal Tax	9,600

[Panjab B.Com. April, 1996]

[**Hints :** 5 units used for own business—NIL ; 2 units let out for non-residential purposes—Rs. 7,200 ; 1 unit let out for residential purposes—Rs. 720]

Profits and Gains of Business or Profession

Q. 38. Mr. X acquired a patent right in 1991-92 for Rs. 7,00,000. During 1996-97 it was sold for

(*a*) Rs. 3,00,000; or

(*b*) Rs. 5,00,000; or

(*c*) Rs. 8,00,000.

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Calculate the amount to be allowed or taxable during 1997-98.

[**Hints :** (*a*) Rs. 1,50,000 to be debited; (*b*) Rs. 50,000 deemed as profit; (*c*) Rs. 2,50,000 deemed as profit and Rs. 1,00,000 capital gain]

Q. 39. Mr. Y spent following amount on scientific research. Calculate the amount which he can debit to P & L A/c during previous year 1997-98:

(*a*) salary of staff and other expenses on research conducted before commencement of business

(*i*) relating to own products Rs. 90,000.

(*ii*) on products not related to own business Rs. 1,10,000.

(*b*) Capital Exp. on land required for research Rs. 5,40,000.

(*c*) Capital Exp. on building and plant and machinery required for research Rs. 6,60,000.

[**Hints :** Amount allowed to be debited Rs. 7,50,000]

Q. 40. Mr. Z purchased technical know-how for Rs. 12 lakhs on 1-4-96. How much amount he can debit to P & L A/c during 1996-97 if

(*i*) it was purchased from a state Govt. financed research institution; or

(*ii*) it was purchased from a foreign company.

[**Hints:** (*i*) Rs. 4,00,000 per year for 3 years;

(*ii*) Rs. 2,00,000 per year for 6 years]

Q. 41. Mr. A has started a new business. The cost of project is Rs. 1,80,00,000. He spent

(*i*) on feasibility report	Rs. 2,00,000
(*ii*) on technical survey	Rs. 1,50,000
(*iii*) on financial consultancy	Rs. 2,00,000
(*iv*) on raising capital	Rs. 100,000

How much he can debit during previous year 1996-97 ?

[**Hints :** Amount to be Dr. 45,000]

Q. 42. During 1993-94 Mr. B claimed a bad debt of Rs. 45,000. After going through the claim Assessing Officer allowed only Rs. 30,000. During 1996-97 Rs. 25,000 were recovered from same debtor. Find out the amount which will be taxable during assessment year 1997-98.

[**Hints :** Taxable amount Rs. 10,000]

Q. 43. From the following information of Viswanath, compute the capital gains for the assessment year 1997-98 :

(*a*) Cost of acquisition of residential house in 1983-84 Rs. 3,48,000.

(*b*) Sale consideration on 1.7.1996 Rs. 14,00,000.

(*c*) Cost of acquisition of new house prior to the date of filing the Income Tax return Rs. 3,00,000.

The cost inflation index in 1983-84 and in 1996-97 was 116 and 305 respectively. *[Nagarjuna B.Com. Sept. 1995]*

[**Hints :** Rs. 1,85,000]

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Q. 44. Mr. Raju provides the following data regarding his transaction for the sale of his residential house for the assessment year 1997-98. Compute the amount of capital gain to be included in the total income for the assessment year 1997-98.

	Rs.
House purchased in 1982-83	4,36,000
Sold in November 1996	17,50,000
Purchased another house in September 1996	3,50,000

Deposited in the Capital Gain A/c Scheme in January 1997 Rs. 4,00,000.

The cost of inflation index for 1982-83 and 1996-97 was 109 and 305 respectively. *[Nagarjuna B.Com. March,1995]*

[**Hints :** Rs. 1,80,000]

Q. 45. Murli gets a house from his uncle under a will on 15th November, 1983, the fair market value on that day being Rs. 1,25,000. His uncle had bought the house for Rs. 25,000 in year 1962 and its fair market value on 1-4-81 was Rs. 54,000. His uncle spent Rs. 10,000 in the year 1972-73 and Rs. 15,000 in the year 1982-83 on its improvement. Murli also spent Rs. 5,000 on the improvement of house in 1985-86. The said house is sold for Rs. 2,58,000 on 15th October 1996. Find out capital gains accruing from the sale of house. Cost Inflation Index numbers for the year 1981-82, 1982-83, 1985-86 and 1996-97 were 100, 109, 133 and 305 respectively.

[**Hints :** L.T.C. Gains Rs. 39,862]

Q. 46. Ram sells a residential house in Bombay for Rs. 5 lakhs on May 1st, 1996, its cost of acquisition in 1981 being Rs. 1 lakhs. On July 20th, 1996 he purchased a new residential house for Rs. 2 lakhs in Meerut. On June 15, 1997, he deposited Rs. 70,000 in the Capital Gains Account Scheme. Compute the amount of exempted capital gain under the Income-Tax Act. C.I.I. for 1981-82 is 100 and for 96-97 is 305.

[Algappa University M.C.S. August, 1995]

[**Hints :** u/s 54 Rs. 1,95,000; u/s 54(2) —NIL]

Q. 47. Mr. P holds 500 shares of ABC Ltd. which were allotted to him on 22-4-1988 @ Rs. 30 per share. On 22nd July, 1996 ABC Ltd. made right issue to the existing shareholders at the rate of one share for every five shares held @ Rs. 20 per share. Mr. P, instead of exercising his right to obtain right shares, has exercised his right of renouncement by renouncing the said right entitlement in favour of Mr. Q @ Rs. 13 per right share entitlement on 4th August, 1996.

Determine the nature and amount of capital gain, if any, taxable in the hands of Mr. P. What will be the cost of acquisition of shares purchased by Mr. Q. *[C.A. Inter Nov. 1995]*

[**Hints :** STC Gain Rs. 1,300; Cost per share for Mr. Q Rs. 33]

Q. 48. Anand, received in cash the following income as interest (net) on securities during the previous year ending 31st March, 1997:

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Rs. 3,600 as interest on less-tax Government Securities.

Rs. 3,600 as interest on debentures issued by the local authority.

Rs. 3,520 as interest on debentures of Meghdoot Ltd. (Not listed at any stock exchange).

Rs. 3,510 as interest on debentures of Mercury Co. (listed).

Determine the interest on securities under the head income from other sources for the assessment year 1997-98, assuming that interest is paid in each case on 30th June and 31st December. Bank charged 2% commission on net amount of int. realised. *[Nagarjuna B.Com March, 1995]*

[**Hints :** Income from other sources Rs. 16,015]

Q. 49. From the following particulars for the year ended 31-3-97, compute the income of Surya Bhaskaram, under the head "Income from other sources":

	Rs.
Dividends (Net)	24,000
Dividends (Gross)	12,000
Dividend collection charges	300
Rent from Buildings and Machinery	30,000
Depreciation on buildings	4,000
Insurance on buildings	1,600

[Nagarjuna B.Com. Sept. 1995]

[**Hints :** Income from other sources Rs. 66,100]

Q. 50. The following investments are held by Mr. Rao on 1-4-1996 :

(*a*) Rs. 40,000, 10% Uttar Pradesh Govt. Loan,

(*b*) Rs. 35,000, 8% Preference Shares of a Sugar Mill,

(*c*) Rs. 50,000, 12% Debentures of Vazir Trading Company.

On 1-9-1996, he sold the debentures-cum-interest and purchased Rs. 50,000, 14% debentures-cum-interest of Beauty Trading Co. Interest and Dividends is received half yearly on 1st July and on 1st January every year. Compute income from other sources for the year ending 31st March, 1997. Bank charged commission @ 2% of interest and dividend.

[Osmania B.Com. Nov. 1995]

[**Hints :** Income from other sources Rs. 13,034]

Q. 51. Sri Chowdhary gives you following particulars for P.Y. 1996-97:

(*a*) Agricultural income from Srilanka	Rs. 20,000
(*b*) Interest on Post Office S. B. account	Rs. 1,000
(*c*) Interest on F.D. from Bank of India	Rs. 9,000
(*d*) Rent from Sub-letting Rs. 1,500 and rent Paid on it	Rs. 3,000
(*e*) Dividend from foreign company	Rs. 15,000
(*f*) Winnings from horse race	Rs. 56,000

Compute his income from other sources.

[Bangalore B.Com. April, 1995]

[**Hints :** Income from other sources Rs. 96,000]

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Q. 52. Gross Total Income of Mr. P for the year 1996-97 was Rs. 1,52,000 which included Rs. 10,000 as 1/4 the share from AOP. He made donation to :

(*a*) To P.M. National Relief Fund Rs. 20,000

(*b*) To Delhi hospital for promotion of family planing Rs. 20,000

Compute his total income.

[**Hints :** Deduction u/s 80G Rs. 35,200 Total Income Rs. 1,16,800].

Q. 53. The income of an individual for the year ended 31st March, 1997 consists of the following :

(*a*) Business profits (after setting off Rs. 20,000 paid as donation to a college) Rs. 52,000.

(*b*) One-fourth share from an association of person in which he was a member Rs. 12,000 (gross). The A.O.P. has paid income tax at MMR.

(*c*) Interest on Government Securities Rs. 8,000 (gross).

(*d*) Dividends on shares of Indian Companies Rs. 6,000 (gross).

Compute the total income and amount entitled to rebate of tax u/s 86 for the assessment year 1997-98.

[**Hints :** G.T.I. Rs 86,000; 80L Rs. 14,000; 80·G Rs. 3,600]

Q. 54. Girish is an individual drawing salary of Rs. 70,000 per annum. He is allowed D.A. @ Rs. 2,000 p.m. He enjoys miscellaneous perquisites valuing Rs. 10,000. Income from other sources amounts to Rs. 35,000.

His disbursements are : Rs. 5,000 as premium on a policy of Rs. 40,000. Rs. 800 on a policy of Rs. 10,000 on the life of his minor son. He is member of a recognised provident fund to which he contributes @ 12% with an equal contribution from employer. Interest accruing to his provident fund amounts to Rs. 800 which has been calculated @ 10%. He has deposited Rs. 6,000 in a ten year account of Post Office Cumulative Time Deposit Scheme. He also buys NSC VIII issue for an amount of Rs. 10,000.

He donates Rs. 2,000 to a university.

Compute Total Income and Tax and rebate of income tax.

[*Panjab B.Com. April, 1996*]

[**Hints :** Salary Income Rs. 90,400; Other sources Rs. 35,000, 80G Rs. 1,000 ; Tax Rs. 22,320 ; Rebate u/s 88 Rs. 6,040]

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5 VERY SHORT QUESTIONS

In the light of changes in the sylabii and pattern of examination papers, the question papers are being divided into various parts—Objective Type Questions, Very Short Questions, Short Questions and Full questions carrying 1%, 2%, 5%, 10% or 20% marks. The previous four chapters of this part of the book deal with questions carrying 20%, 15%, 10% and 5% marks. This chapter shall deal with only those questions which carry 1% or 2% marks.

5.1. Basic Concepts : *The following questions are to be answered in not more than 4 lines*

(i) Ordinary assessee
(ii) Deemed assessee
(iii) Assessee in default
(iv) Average rate of tax
(v) Hindu Undivided Family
(vi) Association of persons
(vii) Body of individuals
(viii) Artificial Juridical Person
(ix) Assessment year
(x) Previous year for new business
(xi) Previous year of continuing business
(xii) Taxability of income of a non-resident from shipping business
(xiii) Taxability of income of discontinued business
(xiv) What will be the previous year in relation to assessment year 1997-98 for a business which commences its operations on 1.1.1997 ?

[Hints : U/S 3 for assessment year 1997-98 his previous year shall be the period between 1.1.1997 to 31.3.1997. In future he shall have to close his accounts on 31st March every year]

(xv) Mr. X discontinued his business on 15.11.1996 and his profit for the period between 1.4.1996 to 15.11.1996 was Rs. 1,69,000. State the assessment year during which his income shall be assessed to tax ?

[Hints : Any person whose business has been discontinued during the previous year, shall be assessed to tax in the same year in which business has

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been discontinued. In above case profit of Rs. 1,69,000 shall be assessed to tax in the assessment year 1996-97 itself.]

5.2. Agricultural Income and assessment : *Explain the following in 3-4 lines :*

(i) Income from a process carried on to make the produce marketable.

(ii) Income from agricultural house property

(iii) Relationship between land and income,

(iv) Meaning of Cultivation of land

(v) Agricultural income from outside India

(vi) Meaning of net agricultural income

(vii) Meaning of non agricultural income

(viii) Conditions for integration

(ix) When agricultural income is not to be integrated ?

(x) For which persons agricultural income is to be integrated ?

(xi) Compute agricultural income :—

Rent from agricultural house property	Rs. 60,000
Taxes paid to State Govt.	Rs. 3,000
Repairs of house property	1/5th of Rental value

[Hints : Rs. 45,000]

(xii) Compute agricultural income from cultivation of land :

	Rs.
Sale proceeds of agri. produce	1,60,000
Depreciation of equipment	6,000
Labour Charges	24,000
Cost of seeds	6,000
Cost of fertilisers	3,000
Electricity Charges	12,000

[Hints : Rs. 1,09,000]

(xiii) Compute agricultural income from rent of land used for cultivation :

Rent for 10 hectares of land @ Rs. 10,000 per hectare	
Expenses on collection of rent	Rs. 6,000
State Govt. Taxes for land	Rs. 3,000
Depreciation of Tubewell installed by owner	Rs. 4,000

[Hints : Rs. 37,000]

(xiv) Mr. X is owner of a tea estate and tea factory. During the year sale proceeds of manufactured tea was Rs. 16,60,000. Expenses incurred on producing and manufacturing tea were Rs. 8,40,000. Compute his agricultural income from tea.

[Hints : 60% of (16,60,000 – 8,40,000) Rs. 4,92,000)]

(xv) Compute tax liability of Mr. X for the assessment year 1997-98

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if his non agri. income is Rs. 60,000 and agri. income is Rs. 40,000.

[Hints : Rs. 6,000]

5.3. A. Capital and Revenue : *Explain the following in four lines each :*

(i) Magnitude of amount—its effect on distinction between capital and revenue receipts.

(ii) Payment made out of capital is capital receipt or not ?

(iii) Effect of nature of asset sold on determination of nature of receipts.

(iv) Effect of substitution of income on determination of receipts.

(v) Compensation recevied on surrender of right is capital or revenue receipt ?

(vi) Compensation received for breach of contract is capital or revenue receipt ?

(vii) Compensation relating to stock in trade is capital or revenue receipt ?

(viii) Nature of subsidies or grants received ?

(ix) Following are capital or revenue receipts :

(a) Compensation received for acquiring Zamindari Rights,

(b) Amount received from Government for use of requisitioned premises ?

(x) Following are capital or revenue receipts :

(a) Damages received by an employee who is wrongly dismissed ?

(b) Lumpsum royalty received in advance from a publisher ?

B. Capital and Revenue Expenses : *Explain the following in not more than four lines each :*

(i) Effect of nature of asset acquired on nature of expenditure.

(ii) Effect of nature of liability discharged on nature of expenditure.

(iii) Expenditure on acquiring an asset for use in business.

(iv) Nature of payment to be determined in the hands of payer only.

(v) Determine whether the following are capital or revenue expenses ?

(a) Cost of reconstructing, refurnishing etc. of a business building.

(b) Ordinary repairs of residential houses allotted to employees.

(vi) Determine whether the following are capital or revenue expenses ?

(a) Price paid for purchase of partner's share.

(b) Amount paid to valuer as fee for assessing the value of business assets.

(vii) Determine whether the following are capital or revenue expenses ?

(a) Expenses on foreign tour to acquire new professional knowledge.

(b) Amount paid to preserve and protect business assets, interest and reputation.

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C. Capital and Revenue Losses : *Explain the following in not more than 4 lines each :*

(i) Loss of cash
(ii) Embezzlement by an employee,
(iii) Loss due to termination of agency,
(iv) Loss by theft from working place during working hours and non working hours,
(v) Determine whether the following are capital or revenue losses :
  (a) Loss of cash by snatching from cash counter,
  (b) Loss of cash while going to bank to deposit it as a routine.

5.4. A. Basis of Charge : A Determination of status. *Explain the following in not more than 4 lines each :*

(i) Conditions given u/s 6(1)(a) and 6(1)(b) for determination of residential status,
(ii) Explanation given u/s 6(1)(b),
(iii) Determination of status of HUF,
(iv) Condition for determining status of not ordinarily resident,
(v) Determination of status of a company,
(vi) Determination of status of artificial juridical persons,
(vii) Mr. A left india for the first time on 31st Dec. 1996. Determine his residential status for the previous year 1996-97.
(viii) Mr. a came to India for the first time on Nov. 6, 1995 and left india on 13th May 1996. He again came to India on 13th Oct. 1996 and left India on 4th April 1997. Determine his status for the previous year 1996-97.

[Hint : R but NOR]

(ix) Mr. X is selected for a job in Nigeria and his agreement has been approved by the Govt. of India. He left India on 1st Oct. 1993 and came back on 30th Sept. 1996. Now he is in India. Determine his status for the previous year 1996-97.

[Hint : R but NOR]

(x) Mr. Ram Yadav is Karta of HUF having property in India and Mauritus. He stayed in India only for 61 days to visit various temples during 1996-97. Determine the status of HUF.

[Hint : Non Resident]

B. Incidence of tax : *Explain the following in not more than 4 lines :*

(i) Incomes to be included in the total income of a Resident u/s 5(1)
(ii) Incomes to be included in the total income of a Non-Resident u/s 5(2)
(iii) Incomes to be included in the total income of a Resident but not ordinarily resident u/s 5 (1) explanation (c)
(iv) Explain the term incomes received in India.

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(v) Explain the term incomes deemed to be received in India.
(vi) Explain the term incomes accruing or arising in India.
(vii) Explain the term incomes deemed to accrue or arise in India.
(viii) Explain the term incomes accruing and received outside India.
(ix) Explain the term incomes accruing and received outside India but from a business controlled from or profession set up in India.
(x) Explain and give treatment of past untaxed income brought into India during relevant previous year.
(xi) Give treatment of salary received outside India by a private sector and government employee.
(xii) Treatment of income from transfer outside India of a asset situate in India.
(xiii) Income from purchase of goods in India for the purpose of exports.
(xiv) Income from a business connection in India.
(xv) Income from transaction part of which takes place in India and part outside.
(xvi) Income from pension received outside India for services rendered in India.
(xvii) Income from shooting of a picture in India by a non-resident non-citizen.

Discuss the taxability of following (each case separately) for R, NOR and NR

(xviii) Salary of Rs. 1,20,000 received by a Govt. employee for working in Bhutan.
(xix) Salary of Rs. 1,20,000 received by a private employee for working in London.
(xx) Income of Rs. 69,000 received in Nepal from Pfizer (India) Ltd.
(xxi) Profit from business in Canada but controlled from India (1/3 received in India) Rs. 84,000.

5.5. Exempted Income : *Answer the following in not more than 4 lines each :*

(i) Casual Incomes — only exempted limits
(ii) Income of NRIs from bonds, shares, securities and interest thereon.
(iii) Exemption of leave travel concession u/s 10(5).
(iv) Passage Money received by a non citizen employee
(v) Limits for exemption of gratuity to an employee covered under Payment of Gratuity Act.
(vi) Limits for exemption of gratuity for government and semi-govt. employee.
(vii) Limits for exemption of gratuity for an employee not covered under Payment of Gratuity Act.
(viii) Limits for exemption of commuted value of pension.
(ix) Limits for exemption of amount received under Voluntary Retirement Scheme u/s 10(10C).

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(x) Which categories of employees are covered under exemption u/s 10(10C)
(xi) What are the limits for exemption of retrenchment compensation u/s 10(10B)
(xii) What are the limits for exemption of allowances given to MP/MLA/ MLC.
(xiii) Exemption of income of a minor child clubbed with income of either parent.
(xiv) Name any two zones notified as Tax Free Zones u/s 10A
(xv) Which benefits (Any Two) are withdrawn on claim of benefit u/s 10B.

COMPUTATION OF TOTAL INCOME

5.6. Income under the head Salaries : *Answer the following in not more than 4 lines* :

(i) Relationship of employer and employee
(ii) Previous year in case of salaries.
(iii) Salary received after certain deductions.
(iv) Place of accrual of salary.
(v) Salary received by a partner from firm.
(vi) Diversion of salary.
(vii) Amount received by legal heirs of an employee.
(viii) Advance salary received.
(ix) Arrears of salary.
(x) What is Statutory Provident Fund (SPF) ?
(xi) What is Recognised Provident Fund (RPF) ?
(xii) What is Public Provident Fund (PPF) ?
(xiii) Treatment of employer's contribution to RPF.
(xiv) Treatment of interest credited to RPF balance.
(xv) Treatment of refund from URPF ?
(xvi) What is transferred balance of URPF to RPF ?
(xvii) How much is taxable out of transferred balance of URPF to RPF ?
(xviii) Treatment of different types of commission.
(xix) Treatment of allowances and perks received by Govt. employees posted outside India.
(xx) What is treatment of Dearness allowance for tax purposes if it enters or does not enter into pay for service benefits ?
(xxi) Give any four allowances which are fully taxable ?
(xxii) What are the limits for exemption of House Rent Allowance u/s 10(13A) ?
(xxiii) What is the treatment of Trevelling allowance and Conveyance allowance u/s 10(14) ?
(xxiv) What conditions must be satisfied by a non-government employee to claim deduction u/s 16(ii) ?

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(xxv) What are the limits for deduction u/s 16(ii) for a govt. employee ?

(xxvi) What are the limits for deduction u/s 16(ii) for a non-govt. employee ?

(xxvii) What are the provisions of law regarding exemption of medical facilities outside India ?

(xxviii) Give any two perks which are fully exempted ?

(xxix) What is the meaning of Fair Rental Value for valuation of rent free house ?

(xxx) What is the definition of salary for valuation of reft free house ?

(xxxi) How will you calculate the value of rent free house for a govt. employee ?

(xxxii) How will you calculate the value of rent free house for semi govt. employee ?

(xxxiii) How will you calculate the value of rent free house for a private employee ?

(xxxiv) What is to be added in the value of rent free house if furnishings are owned by employer or are hired by employer ?

(xxxv) Name any 4 obligations of employee met by employer which are taxable u/s 17(2)(iv) ?

(xxxvi) Give treatment of insurance premia paid by employer as given u/s 17(2)(v) ?

(xxxvii) What are the conditions for taxability of perks covered u/s 17(2)(iii) ?

(xxxviii) What is the treatment of free use of car owned by employer used fully for personal purposes ?

(xxxix) What are the taxable limits for car partly used for personal purposes and partly for employment purposes if car expenses are met by employer ?

(xl) What are the taxable limits for car partly used for personal purposes and partly for employment purposes if car expenses are met by employee ?

(xli) Give treatment of gas and light facility provided by employer ?

(xlii) Give treatment of servants employed by employee but salary is paid by employer ?

(xliii) Give treatment of gardener provided by employer to employee ?

(xliv) What is the definition of average salary for calculating exemption of gratuity for employees covered Payment of Gratuity Act ?

(xlv) What are the limits for exemption of leave encashment u/s 10(10AA) ?

(xlvi) What is the treatment of refund from RPF for tax purposes ?

(xlvii) What is the treatment of refund from URPF for tax purposes ?

(xlviii) What is the rate of standard deduction u/s 16(i) for female employees ?

(xlix) What is the rate of standard deduction u/s 16(i) for male employees ?

5.7. Income under the Head House Property : *Answer the following in not more than 4 lines each :*

(i) Explain the concept of building as given u/s 22.

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(ii) Explain the concept of ''land appurtenant thereto'' as given u/s 22.
(iii) Who is ''owner'' of house property ?
(iv) Who is deemed as owner of house property ?
(v) What is sub letting ?
(vi) How would you treat the house property used for own business ?
(vii) Which rental value is adopted as Annual Rental Value ?
(viii) What is the treatment of cost of facilities borne by owner.
(ix) What is the treatment of local/municipal taxes ?
(x) What are the conditions for allowing new construction allowance ?
(xi) What are the conditions for not allowing new construction allowance ?
(xii) What is the treatment of house property used for own residence ?
(xiii) Explain the deduction of repairs from house property ?
(xiv) Explain the deduction of annual charge ?
(xv) Explain the deduction of unrealised rent ?
(xvi) Explain the deduction of interest on loan taken for repair, renovate, construct or purchase the house ?
(xvii) How the loss from house property is treated for tax purposes.

5.8. Profits and Gains of Business or Profession — Part I : *Explain the following in not more than 4 lines each* :

(i) Define the term business.
(ii) Define the term profession.
(iii) Explain the term adventure in the nature of trade.
(iv) How would you treat income from speculation ?
(v) How would you treat income from illegal business ?
(vi) What is the treatment of rent of business premises ?
(vii) What is the treatment of capital expenditure on scientific research ?
(viii) What is the treatment of revenue expenditure on scientific research.
(ix) What is the treatment of amount given to an institution engaged in scientific research ?
(x) What is the treatment of expenditure on patent rights ?
(xi) What is the treatment of amount realised on sale of patent rights ?
(xii) What is the treatment of expenditure on technical know-how ?
(xiii) What is the treatment of expenditure on eligible projects ?
(xiv) What is the treatment of expenditure on programme of rural development ?
(xv) What is the treatment of expenditure on programme of conservation of natural resources ?
(xvi) What is the treatment of preliminary expenses ?
(xvii) What is the treatment of bad debts ?
(xviii) What is the treatment of bad debts recovered ?
(xix) What is the treatment of entertainment expenses ?
(xx) What is the treatment of advertisement expenses ?
(xxi) What is the treatment of travelling expenses on emloyees ?

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(xxii) What is the treatment of expenses incurred on raising loans from financial institutions ?

(xxiii) What is the treatment of payments made to relatives ?

(xxiv) What is the treatment of payments exceeding Rs. 20,000 if made in cash ?

(xxv) What are the provisions of section 43B regarding payments of provident fund contributions ?

5.9. Profits and gains — Part II–Depreciation : *Explain the following in not more than 4 lines each* :

(i) What is depreciation ?

(ii) Why depreciation is charged ?

(iii) Concept of ownership of asset for charging depreciation.

(iv) Concept of Block of assets.

(v) Depreciation on cars manufactured outside India.

(vi) Use of asset during previous year for charging depreciation.

(vii) Actual Cost — Concept of subsidy received.

(viii) Unabsorbed depreciation.

(ix) Computation of capital gain when block of asset ceases to exist.

(x) Computation of capital gain when block of asset is deemed to cease to exist.

(xi) Eligibility for claim of Tea Deposit Account.

(xii) How amount deposited under Tea Deposit Account can be withdrawn ?

(xiii) Concept of deemed profit under Tea Deposit Account.

(xiv) Eligibility for claim of reserve for shipping companies.

(xv) What is the restriction on claim of reserve for shipping companies.

5.10. Capital Gains : *Explain the following in not more than 4 lines* :

(i) What is capital asset ?

(ii) Name any two assets which are not regarded as capital assets.

(iii) What is short term capital asset ?

(iv) What is long term capital asset ?

(v) Give any two methods under which an asset can be transferred ?

(vi) What is deemed transfer u/s 45 (2) ?

(vii) What is the treatment when an asset is transferred by an individual to a firm, AOP or BOI ?

(viii) What is the treatment when an asset is transferred by a firm, AOP or BOI to a person ?

(ix) What is the effect of amalgamation on transfer of capital assets ?

(x) What is the effect of amalgamation on transfer of shares ?

(xi) Explain the concept of deemed capital gain u/s 47 ?

(xii) What is indexing of cost of acquisition ?

(xiii) What is the treatment of advance money received and forefeited ?

(xiv) What is the cost of goodwill ?

(xv) When and how Fair Market Value is adopted as cost ?

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(xvi) What is the treatment of cost of improvement ?

(xvii) What are the two conditions for investment of LTCG from residential house to claim exemption u/s 54 ?

(xviii) What are the two conditions for investment of LTCG from any asset to claim exemption u/s 54F ?

(xix) What is the time limit for investment of net consideration to claim exemption u/s 54F ?

5.11. Income from other sources : *Explain the following in not more than 4 lines each :*

(i) Give any two examples of general incomes taxable u/s 56 (1).

(ii) In which year the interim dividend and final dividend are taxable ?

(iii) What are the conditions under which no tax is deducted at source from dividend ?

(iv) Name any two casual incomes which are taxable u/s 56 (1).

(v) Name any two casual incomes which are taxable u/s 56 (2).

(vi) What is a security ?

(vii) What is the treatment of amount deducted by employer towards employees' provident fund or ESI fund ?

(viii) Name any two authorities who can issue a security ?

(ix) Name any two securities whose interest is exempted from tax ?

(x) Name any two securities where no tax is deducted at source ?

(xi) What is tax free non govt. security ?

(xii) What is the rate of standard deduction out of family pension ?

5.12. Aggregation of Income : *Explain the following briefly :*

(i) What is revocable transfer and how income is treated ?

(ii) What is the treatment of salary received by a spouse from a concern in which individual has substantial interest ?

(iii) What is the treatment of income from assets transferred to a spouse without adequate consideration ?

(iv) What is the treatment of income from assets transferred to a third person for the benefit of son's wife ?

(v) What is the treatment of assets transferred without adequate consideration and used in business ?

(vi) What is the treatment of income of a minor child u/s 64 (1A) ?

(vii) What is the treatment of income from self acquired assets transferred to common pool of HUF ?

(viii) What is the treatment of cash credits u/s 68 ?

(ix) What is the treatment of unexplained investments u/s 69 ?

(x) What is the treatment of unexplained money u/s 69A ?

(xi) What is the treatment of unexplained expenditure u/s 69C ?

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5.13. Set off and carry forward of losses : *Explain the following terms very briefly :*

(i) What is the rule regarding inter-source set off of losses ?
(ii) What is the rule regarding inter-head set off of losses ?
(iii) What is the rule regarding set off and c/f of capital losses ?
(iv) What is the rule regarding carry forward of business loss ?
(v) What is the rule regarding carry forward of speculation loss ?
(vi) What is the rule regarding carry forward of unabsorbed depreciation
(vii) What is the rule regarding carry forward of expenses on maintenance of horses ?
(viii) What is the rule regarding carry forward of losses of firms ?
(ix) What is the rule regarding filing of return of loss ?
(x) What is the rule regarding carry forward of losses on succession ?

5.14. Deductions u/s 80 out of gross total income : *Explain the following in not more than 4 lines each :*

(i) Who can claim deduction u/s 80D and at what rate ?
(ii) Who can claim deduction u/s 80DD and at what rate ?
(iii) Who can claim deduction u/s 80DDA and at what rate ?
(iv) Who can claim deduction u/s 80E and at what rate ?
(v) Name any two donations which fully qualify for deduction u/s 80G ?
(vi) Name any two donations which qualify for deduction u/s 80G upto certain limit ?
(vii) Name any two donations for which rate of deduction u/s 80G is 100% ?
(viii) What is the limit prescribed u/s 80G for certain donations ?
(ix) Who can caim deduction u/s 80GG and at what rate ?
(x) Name any two payments which qualify for deduction u/s 80GGA ?
(xi) Give any two conditions to be fulfilled to claim deduction u/s 80HHB ?
(xii) What is the rate of deduction u/s 80HHB ?
(xiii) Give the formula to calculate deduction u/s 80HHC for exporter of manufactured goods ?
(xiv) Give the formula to calculate deduction u/s 80HHC for exporter of goods manufactured by others ?
(xv) Give the formula to calculate deduction u/s 80HHC for exporter of manufactured goods who has issued a disclaimer certificate ?
(xvi) Give the formula to calculate deduction u/s 80HHCA in whose favour a disclaimer certificate has been issued ?
(xvii) What is the rate of deduction u/s 80HHD ?
(xviii) What are the eligibility conditions for deduction u/s 80HHD ?
(xix) What is the rate and conditions for claim of deduction u/s 80HHD ?
(xx) What is the rate and conditions for claim of deduction u/s 80HHE ?
(xxi) What is the rate for claim deduction u/s 80IA in case of setting up of infrastructural facility ?

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(xxii) What is the rate for claim of deduction u/s 80IA in case of setting up of industry in notified backward areas ?

(xxiii) What is the rate for claim of deduction u/s 80IA in case of setting up of a power project ?

(xxiv) Name any four incomes which qualify for deduction u/s 80L ?

(xxv) What is the rate of deduction u/s 80L ?

(xxvi) What is the rate of deduction u/s 80R ?

(xxvii) What is the rate of deduction u/s 80RR ?

(xxviii) What is the rate of deduction u/s 80RRA ?

(xxix) What is the rate and conditions for claim of deduction u/s 80U ?

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